Document electronically
generated from the
United Nations
Optical Disk System

Distr.
GENERAL

UNCTAD/SDD/SHIP/3
8 May 1995

Original: ENGLISH
ARABIC, ENGLISH
FRENCH AND SPANISH ONLY

UNITED NATIONS CONFERENCE ON TRADE AND DEVELOPMENT

Ship finance for developing countries

Report by the UNCTAD secretariat

GE.95-51744

CONTENTS

Chapter		Paragraphs
INTRODUCTION		(i) - (vi)
CONCLUSIONS		(vii - xii)
I.	Updates to the supply and demand situation for the world fleet	1 - 6
	A. Trade and fleet forecasts	1
	B. Balance between supply and demand	2 - 3
	C. Age factors	4
	D. Deletions from and additions to the world fleet	5 - 6
II.	Financial implications	7 - 16
	A. Cost structure	7 - 8
	B. Global shipping capital markets	9 - 10
	C. Capital requirements of developing countries and countries in transition	11 - 12
	D. Freight rate markets and the ability to repay debts	13 - 16
III.	Sources and techniques for ship finance	17 - 29
	A. Sources and techniques for financing ships	17 - 18
	B. The role of governments and development institutions	19 - 25
	C. International and regional banks and financial institutions	26 - 29

INTRODUCTION

(i) The Standing Committee on Developing Services Sectors: Fostering Competitive Services Sectors in Developing Countries: Shipping, in its work programme requested the secretariat to study prevailing ship financing arrangements and consider their adequacy in meeting the requirements of developing countries and countries in transition from central planning.

(ii) In September 1992, the secretariat issued a document entitled "Ship finance for developing countries" (UNCTAD/SHIP/642), which established the requirements and availability of different types of financing arrangements for shipowners in developing countries. While this document has been widely circulated among governments and industry circles, the Standing Committee at its second session did not have the opportunity to consider its findings. Consequently, this report should be considered in conjunction with the previous report on ship financing. It mainly covers new developments that have occurred since late 1992 and their impact on the availability of ship financing for developing countries.

(iii) This report consists of four chapters. Chapter I updates the supply and demand situation for the world fleet. Chapter II focuses on the types and sources of finance for acquisition of ships and contains a review of cost structures, global ship capital markets, an estimate of capital requirements for developing countries and countries in transition and freight rate markets' effect on the ability to repay debt. Chapter III provides an updated overview of ship-financing sources. Finally, chapter IV presents conclusions and recommendations.

(iv) The information used for this report was obtained from the following sources:

(a) responses to the note sent by the UNCTAD secretariat to the States members of UNCTAD (dated 18 August 1994);

(b) responses to a communication sent by the UNCTAD secretariat to selected commercial banks and ship-mortgage banks;

(c) responses to a communication sent by the UNCTAD secretariat to international and regional development banks and other development finance institutions;

(d) responses to a communication sent by the UNCTAD secretariat to selected shipping companies of developing countries;

(e) additional information obtained from published sources.

The responses have been integrated in the appropriate sections of this study. While a larger number of responses would have provided a better basis for analysis, the available information does provide a useful indication of the main features of ship financing in developing countries and countries in transition from central planning.

(v) The UNCTAD secretariat wishes to acknowledge with gratitude the cooperation of Governments and the various organizations that supplied information in response to the note and the communications.

(vi) Furthermore, it should be noted that in response to paragraph C.13 of the work programme of the Standing Committee at its first session, the secretariat also prepared a report on "Preliminary Aspects of Ship Leasing in Developing Countries" (UNCTAD/SDD/LEG/4).

CONCLUSIONS

(vii) The conclusions from the secretariat's previous report on ship financing (UNCTAD/SHIP/642), issued in September 1992, have not changed. However, new information indicates that the demand for ship financing is increasing. Total ship financing for newbuilding is now estimated to be in excess of $30.0 billion, largely due to the increasing capacity requirements to meet the expansion in world seaborne trade, to the continuing ageing of the global fleet and to the resulting need to replace technically obsolete tonnage.

(viii) For developing countries and countries in transition, financing requirements for newbuildings and second-hand tonnage are estimated to exceed $93.3 billion over the 1993-1997 period. These capital requirements will be more difficult to finance because second-hand tonnage usually requires more equity participation than newbuildings, and because the fleet profile for these two country groups consists of many technically obsolete vessels.

(ix) The difficulties for capital markets to meet the growing finance requirements are highlighted by the $3.9 billion gap between traditional sources of finance and investment needs. The deficit can be attributed to the conditions in the freight markets. Specifically, current time-charter rates barely cover operating costs and are insufficient to contribute fully to debt service (repayment of principal and interest). Low freight prices are caused by a structural imbalance found in most sectors of the shipping industry, as surplus tonnage is in excess of 10 per cent and is expected to remain at about 15 per cent to the end of the century.

(x) This imbalance is exacerbated by government subsidy and protection policies that distort shipping markets. In the short run, these programmes may support domestic economic programmes by stimulating shipbuilding and employment opportunities, but in the long run they contribute to excess shipping capacity and operating inefficiencies that are shielded from more competitive ship operators. This results in a chronic structural imbalance and distorted freight rates.

(xi) Conversely, it is not the capital market mechanisms that are deficient. On the contrary, financial institutions have been innovative in structuring loans and tailoring the main variables (term, balloon payments, moratoria, down payments, etc.) to meet the cash flows of borrowers. Thus, the essential issue is the inability of the shipping industry to compete for the limited pool of global capital that can obtain higher yields from more profitable projects. These conditions can only be redressed by reducing the tonnage imbalance and eliminating promotional policies that distort markets by artificial prices or protectionism.

(xii) The basic economic principles are no different for developing countries and countries in transition, and the demands on the shipping capital market are equally stringent. However, consideration of special conditions for developing countries, possibly along the lines of terms called for in UNCTAD (resolution 121 V),[1] may provide "softer" financing terms and could be applied to viable projects that require more flexible debt service schedules.

---

[1] UNCTAD Resolution 121 (V) calls for:

(i) Maximum loan = 90 per cent of the contract price;
(ii) Fixed interest rate = 5 per cent per annum;
(iii) Loan repayment period = 14 years for newbuilding, 10 years for second-hand ships;
(iv) Grace period = three years.

Chapter I

UPDATES TO THE SUPPLY AND DEMAND SITUATION FOR THE WORLD FLEET

The basis for determining ship financing requirements are determined by factors that affect the supply and demand conditions for the world fleet. These topics are briefly reviewed in Chapter 1 and include: seaborne trade forecast; world fleet forecasts; the supply/demand balance of the world fleet; age of the world fleet; deletions; deliveries of newbuildings; and tonnage on order.

A. Trade and fleet forecasts

1. The demand for ship finance is derived from seaborne trade and the need to build shipping capacity. Additions to the world fleet replace obsolete tonnage and provide incremental capacity to meet the demands of the expanding world trade. The forecast for world seaborne trade indicates an annual average growth rate of more than 4 per cent during the 1994-2004 period, with total seaborne trade exceeding 5.5 billion tons by 2004. Oil trades will remain the largest sector, while the fastest growth will be in the container trades. The resulting tanker and container fleet expansion is indicated in graph 1. Fleet capacity requirements to service world seaborne trade are forecast to increase by 28.8 per cent between the years 1994 and 2004. The direct effect on finance will be further demands for capital in global credit markets.

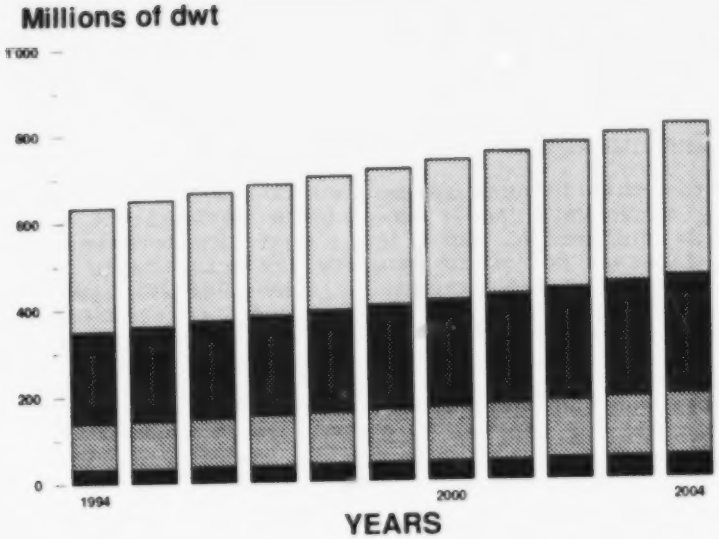
B. Balance between supply and demand

2. The tonnage balance between world supply and demand for shipping capacity not only determines trading prospects but also the volumes of newbuilding. Under conditions of large surplus capacity, shipowners will be reluctant to replace existing vessels. The tonnage oversupply for the world merchant fleet is summarized in table 1. For year-end 1994, 8.8 per cent of the total fleet is surplus, which was well below the peak surplus reached during the 1986-1988 period. However, since 1988, improvement in the overtonnage situation has been slow.

3. Looking to the future (1994-2000), the chronic structural imbalance between total tonnage available and tonnage required is expected to continue. Graph 2 compares the forecasted oversupply situation and indicates that tonnage surplus will be around 15 per cent during this seven-year period. Continuing overcapacity may adversely affect freight markets which in turn may affect the ability of shipowners to generate sufficient cash flow to cover debt-service requirements. If this scenario occurs, lenders will be more selective in granting loans and the net effect may be more stringent financing terms because owners may be required to provide additional security or increase equity participation.

Graph 1

Forecast of world fleet demand



Source: Dri-McGraw-Hill.

Table 1

Tonnage oversupply in the world merchant fleet, 1987-1994
(Million dwt and percentages)

	1987	1988	1989	1990	1991	1992	1993	1994
	Million dwt							
World merchant fleet (as at mid-year)	632.3	627.9	638.0	658.4	683.5 c/	694.7 c/	710.6 c/	719.8 c/
Surplus tonnage a/	101.1	83.4	62.3	63.7	64.2	71.7	72.0	63.4
Active fleet b/	531.2	544.5	575.7	594.7	619.3	623.0	638.6	656.4
	Percentages							
Surplus tonnage as a percentage of the world merchant fleet	16.0	13.3	9.8	9.7	9.4	10.3	10.1	8.8

Sources: Shipping Information Services of Lloyd's Register of Shipping and Lloyd's of London Press Ltd.; *Lloyd's Shipping Economist* (London), various issues.

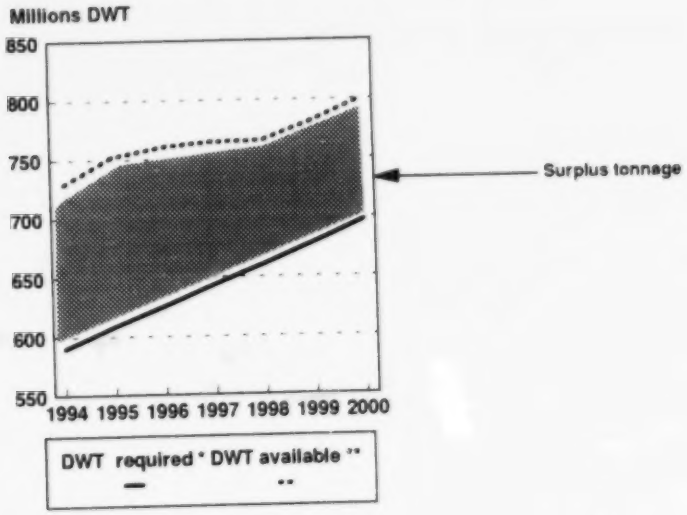
a/ Estimates of average year figures. Surplus tonnage is defined as tonnage which is not fully utilized due to slow steaming, lay-up status or because it is lying idle for other reasons.

b/ World fleet minus surplus tonnage.

c/ Year-end figure.

Graph 2

Total fleet supply/demand, 1994-2000



Source: DRI/McGraw-Hill.

Note: * World fleet requires operating at 90 per cent capacity.
** dwt available less scrapping plus newbuildings.

C. Age factors

4. The age of the world merchant fleet is another important factor affecting new ship construction and financing needs. Although ships may have an operating life in excess of 20 to 25 years, economic obsolescence often becomes a factor after 15 years. This occurs because the costs of maintenance and repairs escalate with age, insurance costs are higher and more modern vessels are more competitive in commercial markets. Table 2 provides the age distribution of the world merchant fleet at year-end 1994. The average age for the world is 15.00 years, as compared to 15.05 years in 1993. In the fleets of developing countries and countries in transition, 45.7 per cent of their total fleets is over 15 years old. In short, these ageing fleets will require increasing replacement tonnage over the next five years to retain existing market shares.

D. Deletions from and additions to the world fleet

5. Deletions from the world fleet reduce the supply of tonnage available. Tonnage sold for demolition remains high, with over 20.77 million dwt broken up in 1994. With the exception of the record year, 1986, when 31.2 million dwt was scrapped, the percentage of the world fleet sold for breaking remains at about 2 per cent, rising to 2.9 per cent in 1994. During the 1993 and 1994 period, the tanker sector represented over 60 per cent of the total tonnage sold for demolition.

6. Conversely, delivery of vessels from shipyards and newbuilding contracts add to the present and future supply of world tonnage. For the former, an 18.7 per cent increase over the previous year occurred in 1993. For the latter, newbuilding contracts almost doubled in dwt terms from 1992 to 1993, and by mid-year 1994 over 40 million grt were on order.[2]

---

[2] Institute of Shipping Economics and Logistics (Bremen), 1994, No. 8/9.

Table 2

Age distribution of the world merchant fleet by type of vessel as at 31 December 1994

(Percentage of total in terms of dwt)

Country grouping	Type of vessel	Total	0-4 years	5-9 years	10-14 years	15 years and over	Average age (years) a/	Average age (years) 1993 a/
World total	All ships	100	15.2	14.7	17.6	52.5	15.00	15.05
	Tankers	100	19.7	11.2	10.3	58.8	15.35	16.86
	Bulk carriers	100	12.1	17.7	23.5	46.7	14.58	13.61
	General cargo	100	7.5	13.0	19.4	60.1	16.61	15.03
	Containerships	100	24.7	21.3	18.4	35.6	12.03	12.82
	All others	100	14.7	16.6	21.6	47.1	14.41	14.14
Developed market economy countries	All ships	100	14.7	16.3	18.7	50.3	14.75	14.44
	Tankers	100	15.2	10.3	11.3	63.2	16.29	16.65
	Bulk carriers	100	11.4	20.5	26.1	42.0	14.04	12.70
	General cargo	100	12.5	19.6	21.4	46.5	14.42	13.26
	Containerships	100	28.0	19.9	17.1	35.0	11.71	13.07
	All others	100	16.5	20.8	22.0	40.7	13.38	13.17
Major open registry countries b/	All ships	100	16.1	10.4	14.1	59.4	15.81	15.88
	Tankers	100	23.5	8.5	7.5	60.5	15.28	17.26
	Bulk carriers	100	8.7	10.1	19.9	61.3	16.76	15.22
	General cargo	100	6.0	13.1	20.0	60.9	16.84	14.34
	Containerships	100	26.9	21.5	16.2	35.4	11.78	13.73
	All others	100	16.5	17.1	16.8	49.6	14.46	14.11
Subtotal	All ships	100	15.3	13.8	16.8	54.1	15.19	15.23
	Tankers	100	18.9	9.5	9.6	62.0	15.84	16.89
	Bulk carriers	100	10.2	15.8	23.3	50.7	15.26	14.13
	General cargo	100	9.8	16.9	20.8	52.5	15.43	13.91
	Containerships	100	27.7	20.3	16.9	35.1	11.73	13.32
	All others	100	16.5	19.8	20.6	43.1	13.67	13.55
Countries of Central and Eastern Europe	All ships	100	4.9	15.6	19.2	60.3	16.76	14.87
	Tankers	100	1.0	14.7	23.6	60.7	17.24	14.13
	Bulk carriers	100	5.4	17.1	21.4	56.1	16.22	13.58
	General cargo	100	5.7	14.0	16.0	64.2	17.14	16.20
	Containerships	100	0.0	28.0	33.6	38.4	14.44	11.29
	All others	100	7.0	16.1	15.6	61.3	16.63	15.56
Socialist countries of Asia	All ships	100	7.8	11.5	14.6	66.1	17.26	16.66
	Tankers	100	14.6	10.5	14.5	60.4	16.06	17.38
	Bulk carriers	100	8.7	12.8	15.6	62.9	16.78	16.23
	General cargo	100	3.5	8.8	12.9	74.8	18.69	17.40
	Containerships	100	11.4	25.0	20.5	43.1	13.92	10.54
	All others	100	3.4	4.7	11.4	80.5	19.48	19.04
Developing countries (excluding open registry countries)	All ships	100	13.5	20.1	19.8	46.6	14.31	14.35
	Tankers	100	16.3	14.2	11.1	58.4	15.50	16.61
	Bulk carriers	100	13.7	31.8	27.1	27.4	11.78	11.12
	General cargo	100	3.4	9.1	17.6	69.9	18.20	16.34
	Containerships	100	31.1	19.7	16.5	32.7	11.18	12.78
	All others	100	13.2	10.3	27.6	48.9	15.06	15.09

Source: Compiled on the basis of data supplied by Lloyd's Maritime Information Services Ltd. (London).

a/ To calculate average age, it has been assumed that the ages of vessels are distributed evenly between the lower and upper limit of each age group. For the 15-years-and-over age group, the mid-point has been assumed to be 22 years.

b/ Including Malta and Vanuatu.

Box

Maritime sector driven by supply

Lloyd's Maritime has carried out research to determine the major factors that influence the marine sector. Although the conventional theory is that the industry's fortunes follow the general economic cycle, market analysts know that the correlation between economic cycles and freight rates is tenuous. The Lloyd's Maritime work establishes supply as a major driving force in the industry.

The research identifies the main influences in the determination of freight rates by analysing the markets over a 30-year period and by fixing relationships between freight rates, economic growth, shipping supply and shipbuilding prices.

The research assessed the relationship between GDP and total world trade. It shows that the volume of cargo shipped by sea decreases at a time of economic slow-down, but the correlation between the two is less than would be expected. From the analysis it is notable that despite several periods of economic downturn, the supply of tonnage has only decreased in 3 of the last 30 years.

Lloyd's Maritime examined the new construction market to see how this responded to changes in the shipping markets. Owners tend to order in rising markets and have their vessels delivered in falling markets. This is the worse scenario for owners of new vessels, as it is in the first few years of a vessel's life that the highest return on investment is required. The need for cash flow to service loans and capital repayments results in owners operating their older vessels for longer than they would like to in a perfect market. The return on investment required for these vessels to generate positive cash flow is less than that for newbuildings. As the market is dominated by these vessels, they tend to set the market rates.

The conclusion of the detailed analysis is that the shipping markets are supply driven. Freight rates only tend to increase substantially at times when supply and demand come into equilibrium. At such times, additional orders tend to be placed for new tonnage, which leads to yards increasing their prices as the supply of available building capacity tightens. This encourages further orders for concern over long-term increases in building costs and the ability to remain competitive in the future.

As a consequence of a number of related factors, shipping markets have been characterized by longer periods of relatively poor return on investment, with only reasonably short periods of high returns. Lloyd's Maritime has called this the "Heartbeat Theory".

Source: Lloyd's Maritime Information Services Ltd. (London), *Review*, November 1993.

Chapter II

FINANCIAL IMPLICATIONS

The impact of the trends in world trade and changes in the world merchant fleet have a direct effect on ship financing. These aspects are covered in this chapter with a review of cost structures, global ship capital markets, an estimate of capital requirements for developing countries and countries in transition and freight rate markets' effect on the ability to repay debt.

A. Cost structure

7. The costs of shipping companies are divided into three main elements - capital, operating and voyage costs. Capital charges, consisting of interest charges and principal repayment, are fixed, while operating and voyage costs are variable. Allocation of these fixed and variable costs for developing country vessels are estimated in table 3.

Table 3

Annual cost structure by vessel types
(Millions of US dollars)

	Conventional breakbulk ship (10,000 dwt)	Combination carrier (16,000 dwt)	Container vessel (1,500 TEU)
Annual costs			
Capital	0.9	2.1	6.8
Operations	1.8	2.9	3.3
Voyage	1.6	2.4	3.5
TOTAL	4.3	7.4	13.6
Capital cost as percentage of total	20.9	28.4	50.0

Source: World Bank, Seatrade, Logistics and Transport, 1992.

8. The capital cost proportion varies between 21 per cent for a conventional breakbulk ship to 50 per cent for container vessels. Moreover, these financial costs are ongoing regardless of market conditions or the activity status of the vessel. Therefore, even if the ship is idle or in lay-up, the debt service (interests and principal) will continue until the loan is amortized.

B. Global shipping capital markets

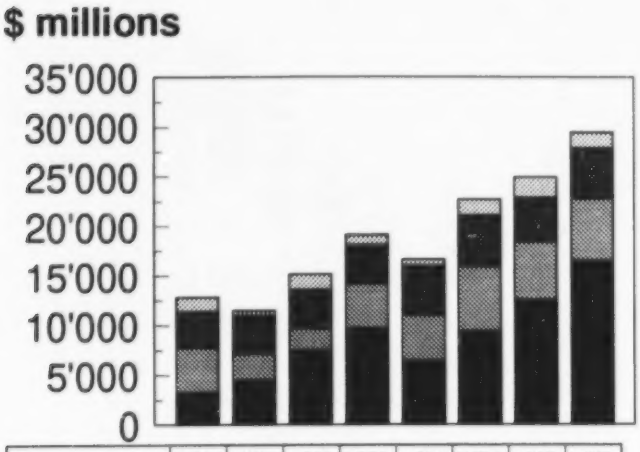
9. The 1990-1997 world demand and supply for shipping capital is summarized in graph 3. Demand (graph 3a) is estimated to be $29.4 billion by 1997 and will average about $23.4 billion during the 1994-1997 period. The bulk sectors (tanker and dry) will require the most capital but the cruise market will increase the fastest. The rapid escalation in demand (up over 130 per cent), or 14.9 per cent per annum, places considerable pressure on global capital markets to provide additional finance for shipping.

10. The supply of capital (graph 3b) indicates that world capital markets have responded to the rising demand. For example, total capital supplies increased 77.8 per cent from 1990 to 1994. Primary sources of capital come from five principal financial markets: (1) private debt; (2) public equity; (3) public debt; (4) banks; and (5) shipyard credits. Shipyard credits, which are often supported by government assistance and subsidy programmes and banks are the two largest sources. There remains, however, a significant gap between the supply and demand for global shipping capital. Graph 4 illustrates the deficit that is expected to exceed $3.9 billion by 1997.

Graph 3

Comparison of shipping capital demand and supply

(a) Capital demand by vessel types



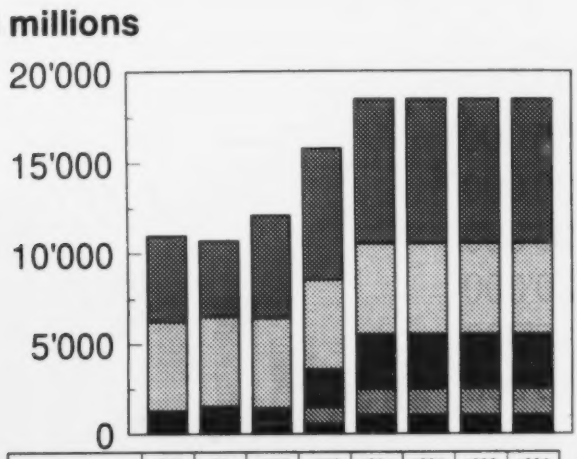
	1990	1991	1992	1993	1994	1995	1996	1997
Tankers	3'229	4'543	7'566	9'688	6'446	9'383	12'504	16'497
Dry Bulk Carriers	4'480	2'585	2'166	4'431	4'523	6'508	5'838	6'246
Liners & Misc.	3'640	3'907	3'850	3'940	5'000	5'200	4'520	5'140
Cruise	1'451	418	1'529	1'043	639	1'577	2'075	1'600
Total Demand	12'800	11'453	15'111	19'102	16'608	22'668	24'937	29'483

Source: Citicorp Securities, Inc., October 1994.

Note: Figures for 1994-1997 average.

Graph 3 (continued)

(b) Sources of shipping capital



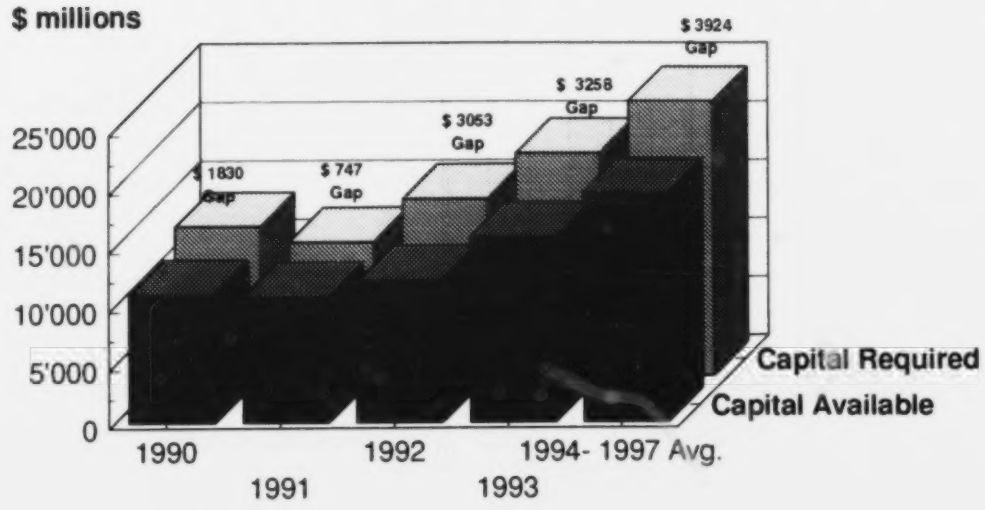
	1990	1991	1992	1993	1994	1995	1996	1997
Private Debt	1'000	1'000	500	500	1'000	1'000	1'000	1'000
Public Equity	200	225	250	993	1'500	1'500	1'500	1'500
Public Debt	50	300	676	2'050	3'000	3'000	3'000	3'000
Banks	5'000	5'000	5'000	5'000	5'000	5'000	5'000	5'000
Shipyard Credit	4'720	4'181	5'653	7'201	8'000	8'000	8'000	8'000
Total Supply	10'970	10'706	12'079	15'744	18'500	18'500	18'500	18'500

Source: Citicorp Securities, Inc., October 1994.

Note: Figures for 1994-1997 average.

Graph 4

Gap in supply and demand for shipping capital



Source: Citicorp Securities, Inc., October 1994.

C. Capital requirements of developing countries and countries in transition

11. Since the previous UNCTAD report entitled "Ship finance for developing countries" (UNCTAD/SHIP/642), new conditions have arisen. The scope of this report is expanded to cover investment requirements in both developing countries and countries in transition. Moreover, market conditions have changed. Most importantly is a decline in shipbuilding prices. For example, the percentage change in 1992-1994 for an 80,000 dwt tanker is down 2.4 per cent, while a handy-size bulk carrier declined 12.5 per cent and a 2,500 TEU containership 18.6 per cent. Conversely, second-hand tonnage prices increased over the 1992-1994 period.

12. In estimating the capital requirements for developing countries and countries in transition, selected assumptions were made. The starting point is the 1993 deadweight by principal ship type. The age profile was then examined and the percentage of vessels over 15 years old were identified as needing replacement within the next 5 years. This deadweight less tonnage already on order determines the newbuilding deadweight requirements and a cost per deadweight ton was applied to each vessel type. However, about 30 per cent of the requirement is purchased in the second-hand market. This option serves to reduce total investment requirements, but additional tonnage to cover trade growth mitigates the decrease in capital required. Table 4 adjusts the total dwt and capital requirements by applying moderate annual average growth factors (5.7 per cent)[3] to determine the 1993-1997 requirements apportioning purchases between newbuildings (70 per cent) and second-hand tonnage (30 per cent), and applies current (1994) prices to obtain the $93 billion investment requirement for the five-year period.

---

[3] Average annual growth for developing countries fleets during 1980-1993 is 7.2 per cent.

Table 4

Total capital requirement for ship acquisitions by developing countries and countries in transition over the 1993-1997 period

Ship type	Tonnage in excess of 15 years old (1993)	1993-1997 total tonnage required (millions dwt)	Investment required for newbuildings (billions US$)	Investment required for used ships (billions US$)	Total capital required (billions US$)
Tankers	33.6	38.2	15.40	2.18	17.58
Bulk carriers	24.7	31.8	9.97	3.30	13.27
General cargo	27.7	33.7	37.11	6.33	43.44
Containerships	1.9	7.0	6.49	1.83	8.32
All others	7.9	9.188	8.88	1.90	10.78
Totals	95.80	119.89	77.85	15.54	93.39

Source: Compiled on the basis of data provided by Lloyd's Maritime Information Services Ltd. (London), Lloyd's Shipping Economist and UNCTAD secretariat calculations.

D. Freight rate markets and the ability to repay debts

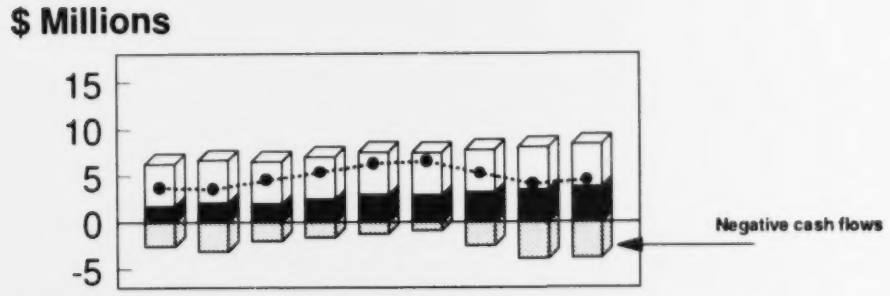
13. The ability to repay principal and interest are a key lending factor. Financial institutions will closely examine estimates of ship project cash flows to determine the financial viability of the investment and debt-service requirements. In practice, this means that the annual revenues less operating costs must provide an operating surplus to cover the capital repayment schedule over the life of the loan.

14. The impact of depressed freight rates is to reduce gross revenues and decrease operating surpluses. This occurs as operating expenses tend to rise with inflation and vessel age and thus margins are squeezed. For example, during the 1986-1992 period, time-charter revenues in the tanker, dry bulk, container and general cargo sectors were only sufficient to meet operating costs and contribute to only a portion of the annual capital repayment needs.

15. Graphs 5 to 8 illustrate the negative cash flows of four representative vessels. In each case, yearly operating costs, annual capital repayment and annual time-charter revenue are compared. The profitability is calculated by deducting operating or capital expenses from the time-charter revenue and the net results are mostly negative cash flows.

Graph 5

Profitability profile of panamax tanker, 1989-1994

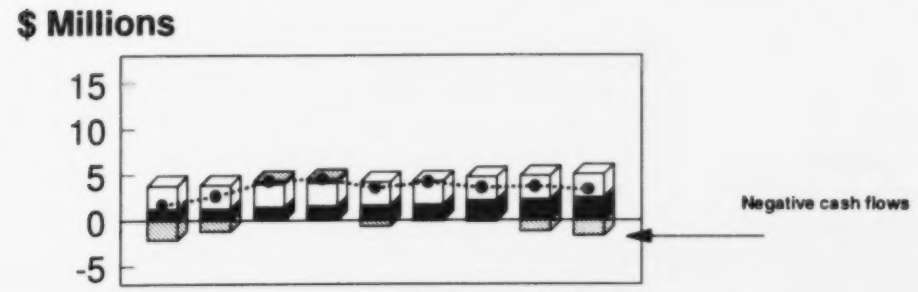


	1988	1987	1988	1989	1990	1991	1992	1993	1994
Operating	1.720	2.090	1.950	2.430	2.940	2.860	3.180	3.448	3.740
Capital	4.570	4.570	4.570	4.570	4.570	4.570	4.570	4.570	4.570
Time charter revenue	3.690	3.540	4.490	5.330	6.240	6.500	5.210	4.060	4.460
Profitability	-2.600	-3.120	-2.030	-1.670	-1.270	-0.930	-2.540	-3.960	-3.850

Source: Drewry Shipping Consultants (London), *Shipping in the 1990s*; *Lloyd's Shipping Economist*, various issues, 1993-1994.

Graph 6

Profitability profile of handy-size bulk carrier, 1989-1994

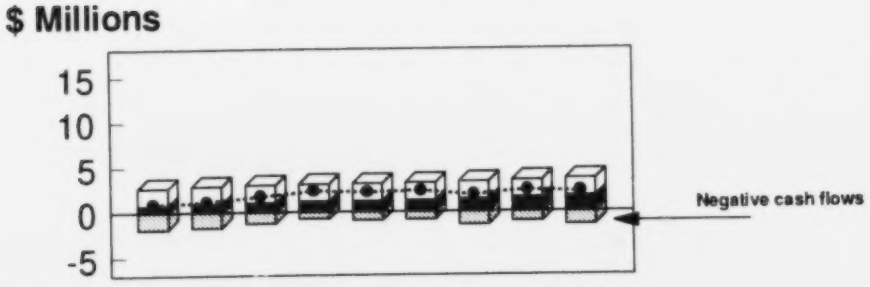


	1988	1987	1988	1989	1990	1991	1992	1993	1994
Operating ■	1.260	1.290	1.450	1.580	1.630	1.710	2.160	2.300	2.470
Capital □	2.540	2.540	2.540	2.540	2.540	2.540	2.540	2.540	2.540
Time charter revenue ●	1.690	2.640	4.290	4.510	3.530	4.160	3.520	3.675	3.307
Profitability ⊡	-2.110	-1.190	0.300	0.390	-0.640	-0.009	-0.090	-1.165	-1.700

Source: Drewry Shipping Consultants (London), *Shipping in the 1990s*; *Lloyd's Shipping Economist*, various issues, 1993-1994.

Graph 7

Profitability profile of general cargo ship 15k dwt, 1989-1994

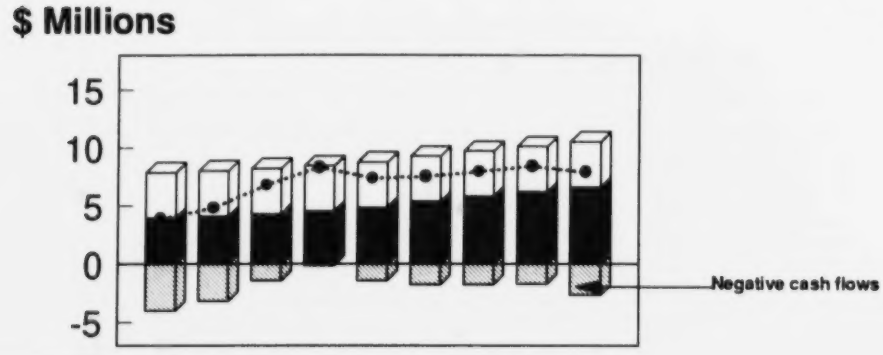


	1986	1987	1988	1989	1990	1991	1992	1993	1994
Operating	0.740	0.900	1.040	1.130	1.160	1.220	1.360	1.500	1.670
Capital	1.930	1.930	1.930	1.930	1.930	1.930	1.930	1.930	1.930
Time charter revenue	0.810	1.150	1.730	2.270	2.140	2.290	1.840	2.345	2.174
Profitability	-1.860	-1.680	-1.240	-0.790	-0.950	-0.860	-1.450	-1.085	-1.426

Source: Drewry Shipping Consultants (London), *Shipping in the 1990s*; *Lloyd's Shipping Economist*, various issues, 1993-1994.

Graph 8

Profitability profile of 2,500 TEU containership, 1989-1994



	1993	1997	1998	1999	1990	1991	1992	1993	1994
Operating ■	3.940	4.090	4.300	4.510	4.840	5.340	5.800	6.185	6.597
Capital □	3.920	3.920	3.920	3.920	3.920	3.920	3.920	3.920	3.920
Time charter revenue ●	3.840	4.820	6.780	8.290	7.370	7.500	7.960	8.396	7.874
Profitability ⊡	-4.020	-3.190	-1.440	-0.140	-1.390	-1.760	-1.760	-1.709	-2.643

Source: Drewry Shipping Consultants (London), *Shipping in the 1990s*; *Lloyd's Shipping Economist*, various issues, 1993-1994.

16. The implications for ship finance is to limit credit because lenders will carefully examine cash flow projections to ensure that debts can be repaid. Moreover, many lenders will insist on greater equity participation by shipowners. For developing countries and countries in transition, this may increase barriers to fleet expansion because less credit will be available and thus the opportunity to renew their fleets with more competitive and modern tonnage may be denied.

Chapter III

SOURCES AND TECHNIQUES FOR SHIP FINANCE

Chapter III provides an updated overview of ship-financing sources. Additional basic details are found in the previous secretariat report entitled "Ship finance for developing countries" (UNCTAD/SHIP/642). The three topics covered are sources and techniques for financing ships, the role of national governments and development institutions and international banks.

A. Sources and techniques for financing ships

17. To finance the estimated $93 billion necessary to replace the fleets of developing countries and countries in transition, shipowners have four broad alternatives: equity, senior debt, subordinate debt and leases. Within these categories are several types of finance option, which are summarized in table 5.

18. The structure of the loan will be a mixture of the financing categories. The main variables include: (1) the down payment; (2) the rate of interest; (3) the loan repayment period; and (4) grace periods on interest and capital repayment. The credit-worthiness of the borrower will determine the apportionment of the options. The criteria for determining the credit-worthiness focuses on the ability to repay and is influenced by markets, tonnage, equilibrium between supply and demand, operating costs and public policy.

B. The role of governments and development institutions

19. Government support programmes for the shipping sector include direct and indirect programmes for shipbuilders and shipowning/operating companies. Most of these programmes serve to reduce capital and operating expenditures through grants and subsidies, and enhance the credit-worthiness of the borrowers by reducing the risk to lenders. The latter occurs when commercial loans are guaranteed by governments or when protectionist measures limit competition and the net result is to increase the probability of repayment. A summary of government assistance by country is found in the Annex.

20. The United States Department of Transportation, Maritime Administration's survey (September 1993) indicates that the largest government subsidiary expenditures were direct support to shipyards. Indirect tax benefits through rapid ship depreciation are another fiscal subsidy that is offered by 38 governments. Also, promotional trade agreements are provided by 40 governments.[4]

21. The United States Federal Ship Financing Program (1994) provides a limited opportunity window (until 1996) for developing countries and countries in transition to obtain long-term financing at more favourable rates and conditions than usually found in capital markets. Although the programme primarily aims to promote the United States merchant marine and United States shipyards, benefits can accrue to qualified foreign shipowners. The eligibility requirement for the Title XI of the Merchant Marine Act, 1936 as amended is generally extended to commercial vessels such as passenger, bulkers, cargo, tankers, tugs, towboats, barges, dredges, oceanographic research, pollution abatement, offshore oil and floating dry docks.

---

[4] Source: United States Department of Transportation, Maritime Administration, Maritime Subsidies, September 1993.

Table 5

Financing options for merchant ships

Finance category	Type of finance	Typical features
Equity	Owner equity	Finance provided by owner from own funds and retained earnings, accumulated depreciation
	Limited partnership	Funds provided by joint venture partners
	Ship fund shares	Shares in company bought privately by individuals or listed on stock exchange
	Public offering shares	Shares sold by subscription on public stock exchange
Subordinate loan	Private placement	Debts with high interest rates and possibly equity rights
Senior debt	Bond issue	Security issued in the capital market
	Commercial bank loan	Mortgages provided by banks may be syndicated between several banks
	Shipyard credit	Loans provided by governments or agencies to assist domestic shipyards
	Private placement	Debt-finance arrangement privately with pension fund, insurance company, etc.
Lease	Finance lease	Long-term tax-effective finance based on sale of ship to company which uses depreciation benefits; may be leveraged.
	Operating lease	

Source: Indian Shipping, vol.XLVI, Numbers 2-3/1994.

22. The Act permits guarantees in an amount not exceeding 87.5 per cent of the actual cost and the maximum guarantee period is the lesser of 25 years or the remaining economic life of the vessel. Amortization in equal payments of principal is usually required; however, other amortization methods, such as a level debt (equal payments of principal and interest) may also be approved if sufficient security is offered, such as long-term charters, reduction of the amount of guarantee and/or the length of the guarantee period. The interest rate of the obligations guaranteed is determined by the private sector. Generally, in establishing the interest rate, the prospective obligee would utilize as a benchmark rate the interest rate carried by the United States Treasury obligations, comparable to the average life of the proposed debt issue.

23. Other countries also provide financial assistance for shipbuilding. These are mostly developed market-economy countries which produced about two thirds

of the deliveries of newbuildings in 1993.[5] For example, the OECD agreement on shipbuilding[6] provides guidelines on export credits for ships. These are important to all countries because about 75 per cent of the world's shipbuilding capacity will be covered by the agreement. Key financing terms, applicable as of 1 January 1996, will be:

(i) a minimum deposit of 20 per cent of the contract price;

(ii) a maximum duration of 12 years from delivery;

(iii) repayment schedule by equal instalments at regular intervals, normally of 6 months and a maximum of 12 months;

(iv) an interest rate at the commercial interest reference rate.

24. The impact on ship financing will be to reduce competition between governments in providing export credit terms. In practice, this means credit subsidies should be eliminated and competition for shipbuilding orders will focus on prices, quality and delivery times. For developing countries and countries in transition, the ability to negotiate more flexible credit terms may decrease and thus financing options may become more stringent.

25. These limitations, however, may be mitigated because the agreement allows participants to offer more flexible financing terms for "genuine aid reasons".[7] This exception requires that: (1) the ship not be operated under an open-registry for the duration of the credit; (2) the ship's ultimate owners reside in the country receiving the credit and that the ship is not a non-operational subsidiary of a foreign interest and is not to be sold without government approval. Moreover, eligibility for concessional or aid credit should not be extended if the project is commercially viable on market terms, respectively those of the Understanding (see foot-note 6). There are two criteria for determining aid eligibility and hence an exemption to the agreement: (1) the inability of the project to generate sufficient cash flow to cover operating costs and to service the capital under the terms of the agreement; and (2) is the exclusion of aid credits to countries whose per capita GNP would make them ineligible for 17- or 20-year loans from the World Bank.[8]

C. International and regional banks and financial institutions

26. In updating the previous finance report, replies from the mail survey indicated that only two regional development banks have made some modifications since the last report (1992).

27. The Islamic Development Bank (IDB) stated that their main features of ship financing are:

1. The IDB leases new ships as well as second-hand ships up to five years old, but preferably not more than three years old, to shipping companies in member countries.

2. The ships are generally financed through leases for a specific period (generally for 8 years) but in any case not more than 10 years. The interest rate for qualified borrowers is 8.5 per cent and the maximum amount of financing is about US$ 20.0 million.

---

[5] UNCTAD, *Review of Maritime Transport, 1993* (TD/B/CN.4/37).

[6] OECD, Council Working Party on Shipbuilding, Understanding on Export Credits for Ships (C/WP6(94)6), Paris, 3 October 1994.

[7] Ibid.

[8] GNP per capita over $2,465 in 1990.

3. At the end of the lease period and on receipt of all the lease rentals, the ownership of the vessel is transferred to the lessee.

4. The vessel is leased against an irrevocable, unconditional guarantee from a first-class commercial bank, acceptable to the IDB.

5. The rental fee of the vessel will be payable in six equal monthly instalments. The first instalment will fall due for payment six months after delivery of the vessel.

6. The lessee will be responsible for the vessel's maintenance and successful operation, as well as for other expenses and claims related to the possession of the vessel.

7. The lessee will buy comprehensive insurance policy for the "stipulated loss value" to cover all possible eventualities for the protection of the asset. A copy of the insurance policy will be sent to the IDB. The insurance policy will be effective from the time of the takeover of the vessel until the payment of the last rental instalment. All claims and disputes, etc., would be pursued by the lessee. The insurance company covering the liabilities must be acceptable to the IDB.

8. Corporate taxes, customs duties and other levies, if any, either on the assets or for the operation or the instalments payable to the IDB shall either be borne by the lessee or shall be given exemption by the Government.

9. The vessel will be registered in the name of the IDB in a country decided upon by the IDB and the lessee. The vessel will be named by the lessee in consultation with the IDB.

10. The latest prices of vessels (available for sale) should always be obtained for guidance from the Baltic Exchange, London, or a similar Exchange in the process of procurement.

28. Information from the African Development Bank (ADB) indicated that ship financing for privately owned and managed enterprises could be made available. In this case, an average payment between 5 and 12 years with variable interest rates may be possible, subject to a full analysis of the project and the credit-worthiness of the borrowers.

29. As stated in the report of September 1992, the World Bank group and its affiliates continue to have limited involvement in ship financing.

Annex

Summary table of maritime subsidy measures

Country	Other aids	Maritime Insurance Aids	Research and Development Aids	Cabotage	Government ownership	Customs duty, levies and	Tax and depreciation benefits	Export aids	Scrap and build aids	Bilateral or trade agreements	Cargo preference requirements	Financing programmes	Restructuring aids	Construction subsidies	Operating subsidies
Algeria		X		X	X					X					
Argentina	X	X		X			X			X	X				
Australia				X	X	X	X	X			X	X		X	
Bahamas				X		X									
Bangladesh		X		X	X					X	X				
Belgium	X		X	X	X	X	X	X		X		X		X	
Brazil		X		X	X	X	X	X		X	X	X			
Canada			X	X			X	X	X						
Chile				X	X	X	X			X					
Colombia		X		X											
Côte d'Ivoire	X	X		X	X					X					
Cyprus	X						X								
Denmark	X		X	X	X	X	X	X	X	X		X		X	
Ecuador				X	X						X				
Egypt	X	X		X			X			X					
Finland			X	X		X	X	X		X		X		X	
France	X		X	X			X	X		X	X		X	X	X
Germany	X		X	X	X	X	X	X		X		X	X	X	
Greece	X			X		X	X	X	X			X	X		
Honduras				X						X					
Hungary				X	X										
India	X	X		X	X		X		X	X	X	X		X	
Indonesia	X			X	X	X				X	X				

Country	Other aids	Maritime Insurance Aids	Research and Development Aids	Cabotage	Government ownership	Customs duty, levies and	Tax and depreciation benefits	Export aids	Scrap and build aids	Bilateral or trade agreements	Cargo preference requirements	Financing programmes	Restructuring aids	Construction subsidies	Operating subsidies
Israel	X	X			X		X			X					
Italy	X	X	X	X	X	X	X	X		X	X	X	X	X	X
Japan	X		X	X	X	X	X	X	X	X		X	X	X	
Kenya	X	X			X						X				
Republic of Korea	X		X	X		X	X	X		X	X	X	X		X
Kuwait					X					X	X				
Malta		X			X		X							X	
Mexico	X	X		X	X	X	X			X					X
Morocco	X	X			X		X			X	X			X	X
Myanmar					X						X				
Netherlands	X		X			X	X	X		X		X	X	X	
New Zealand				X			X								
Nigeria	X	X		X		X				X					
Norway	X		X				X			X		X		X	
Pakistan				X	X		X		X	X					
Panama	X				X		X								
Peru	X	X		X			X			X		X		X	
Philippines				X		X	X			X	X				
Poland	X			X	X										
Portugal				X	X		X			X	X			X	X
Romania	X			X	X					X			X		X
Singapore					X										
South Africa								X		X		X			
Spain	X	X		X	X	X	X	X		X	X	X	X	X	
Sri Lanka	X			X	X	X				X		X			

Country	Other aids	Maritime Insurance Aids	Research and Development Aids	Cabotage	Government ownership	Customs duty, levies and	Tax and depreciation benefits	Export aids	Scrap and build aids	Bilateral or trade agreements	Cargo preference requirements	Financing programmes	Restructuring aids	Construction subsidies	Operating subsidies
Sweden				X		X	X			X		X			X
Switzerland	X						X					X			
Taiwan Province of China				X	X	X	X			X	X	X		X	
Thailand				X		X	X			X	X			X	
Turkey				X			X				X			X	
United Kingdom	X			X	X		X			X			X	X	
United States	X			X		X	X			X	X	X			X
Uruguay				X	X	X	X			X	X	X			
Venezuela				X	X					X	X				

Source: United States Maritime Administration, Maritime subsidies, 1993.

Distr.
GENERAL

UNCTAD/SDD/SHIP/4
10 May 1995

Original: ENGLISH
ARABIC, ENGLISH, FRENCH
AND SPANISH ONLY

UNITED NATIONS CONFERENCE ON TRADE AND DEVELOPMENT

Maritime policy reforms in the New Independent States of the former Soviet Union

Experiences and proposals

Report by the UNCTAD secretariat

GE.95-51620

CONTENTS

Chapter		Paragraphs
Summary		(i) - (viii)
Introduction		(ix) - (xi)
I.	Improving the competitiveness of the national merchant fleets	1 - 20
	A. The necessity to improve competitiveness of national fleets	1 - 4
	B. Measures aimed at fostering competitiveness of NIS national fleets	5 - 20
II.	Privatization of shipping and port operations	21 - 49
	A. Principles of privatization and implementation policies	21 - 33
	B. Some examples of the state of privatization in NIS	34 - 43
	C. Social impact of privatization	44
	D. Legal and institutional framework of privatization	45 - 49
III.	Liberalization of shipping markets	50 - 104
	A. General considerations	50 - 55
	B. Policy instruments affecting market access	56 - 64
	C. Price-based measures aimed at promoting domestic providers of shipping services	65 - 68
	D. Relaxation of government intervention	69 - 93
	E. Other support measures to promote national fleets	94 - 103
	F. Participation in international organizations	104
IV.	Impact of policy reform measures	105 - 123
	A. Impact of policy measures on the participation of national fleets in shipping	107 - 116
	B. Impact on freight rates	117
	C. Impact on quality of services	118 - 120
	D. Impact on management and interaction with other modes of transport	121 - 123

SUMMARY

(i) The maritime industry of the New Independent States of the former Soviet Union (NIS) is undergoing a process of transition from central planning to market-oriented operations.

(ii) In order to undertake this transition successfully, a number of policy measures have been taken by the various NIS aimed at creating functioning maritime transport markets and ensuring the competitiveness of national merchant marines. Specific objectives of various initiatives taken by NIS governments are designed to:

- enhance the ability of national fleets to participate effectively in international shipping according to the principles of free market access, equality and fair competition;
- promote the carriage of national foreign trade cargo by national fleets, thus ensuring - to a reasonable degree - the independence of national foreign trade from foreign shipowners;
- improve the efficiency of national foreign trade by reducing the amount of foreign currency spent on chartering foreign flag vessels and employing modern national vessels;
- create the environment necessary for the development of vital shipping services to conduct foreign trade between nations;
- encourage the development of foreign trade using national sea tonnage.

(iii) In order to improve the competitiveness of national merchant marines, a policy of commercialization and privatization of former State-owned shipping companies is being pursued in the NIS concerned. While privatization as a policy option is being most vigorously pursued in the Russian Federation, other countries such as the Baltic States and the Ukraine have, for the time being, embarked on commercialization programmes only, without initiating a transfer of ownership of national lines to the private sector. Nevertheless, also in the Russian Federation, privatization is hampered by shortcomings in the national capital markets and the lack of institutional arrangements necessary for full-scale privatization.

(iv) Liberalization of shipping markets is part of the ongoing process of economic restructuring that is currently taking place in the NIS, and can be considered a prerequisite for the future development of its fleets. It provides the framework for a reduction in government involvement in shipping and the establishment of commercially viable enterprises, either on the basis of local investment or as joint ventures with foreign partners.

(v) The situation of most NIS shipping industries is difficult. Companies that had enjoyed monopolies in the former USSR trades, today have to face competition without necessarily being prepared for it. The commercialization programmes have forced companies to compete for cargo, yet have not made sufficient provisions for the adaptation of management structures, or for improved access to finance that is necessary to modernize existing fleets.

(vi) One of the most important prerequisites for the successful development of national merchant marines is to attract foreign capital. Measures are thus taken to facilitate the movement of capital, either as equity or as loan capital to the maritime sector of the countries concerned. Facilities offered include the repatriation of profits in freely convertible currencies and protection against nationalization or confiscation.

(vii) A number of policy instruments have been designed to support the process of liberalization, commercialization and privatization. In order to manage this policy reform effectively, backup measures are proposed or implemented that are aimed at supporting and protecting domestic providers of shipping services through subsidies, investment aids, licensing systems, etc.

(viii) At this stage, it is too early to judge the effectiveness of policy measures. None of the countries concerned has, until now, undertaken a

comprehensive analysis of the impact of policy programmes and action. More experience is needed to establish the causal relationship between policy reform and specific market and fleet developments. Furthermore, a certain time-frame is required for shipping companies to undertake the necessary management reform programmes, thus enabling them to compete commercially for cargo, both in national trades as well as cross-trades.

INTRODUCTION

(ix) The Standing Committee on Developing Services Sectors: Shipping, at its second session, reconfirmed and amended its work programme in the field of shipping, port and multimodal transport, adopted at its first session in November 1992. Paragraphs 4 and 5 of the recommendation annexed to the report of the Standing Committee at its second session request the secretariat:

"(a)to undertake a comparative analysis of the shipping sector and related policies in different countries with a view to determining factors contributing to or impeding the development of national shipping industries, including the participation by the private sectors and/or commercialization programmes to increase market orientation and to facilitate provision of competitive shipping services. In doing so, the general economic and social environment in the countries concerned is to be borne in mind;" and

"Given the diversity and the limited experience that has been accumulated so far on the formulation and implementation of progressive liberalization and its impact particularly on developing countries and countries in transition, the Committee requests the secretariat to continue monitoring and reporting on:

(a) Progressive liberalization and associated measures aimed at fostering fair and competitive shipping services;

(b) The results experienced and problems of countries which have liberalized their shipping services;

(c) Measures which countries have adopted, or might consider adopting, to correct problems arising from progressive liberalization;

(d) Prior and/or accompanying measures which might be considered by countries willing to implement progressive liberalization."

(x) In response to this request, the secretariat has prepared this report. It attempts to identify issues that are becoming more crucial in the evolution of shipping policies of the New Independent States of the former Soviet Union (NIS). It focuses on shipping, but, in some cases, such as an analysis of privatization, ports are also involved because they are an essential component of the maritime transport sector. Furthermore, while the report covers all NIS, it draws heavily on developments and experiences of the Russian Federation because of the sometimes limited availability of information. Experiences of other countries of Central and Eastern Europe (CEE) have been taken into account to illustrate specific developments.

(xi) This report has been prepared on the basis of a consultant's study.

Chapter I

IMPROVING THE COMPETITIVENESS OF NATIONAL MERCHANT FLEETS

A. The necessity to improve the competitiveness of national fleets

1. Since the breakup of the COMECON and the USSR, maritime policies and the state of national fleets have changed dramatically. When considering the most striking changes, brief reference has to be made to the former USSR fleet. First, the former single fleet has been broken up and divided among the former USSR Republics. In this way, the new independent States (NIS) have become fleet owners and flag States. Second, the division of the fleet according to ports of call has determined the structure of the emerging national fleets. Thus, for instance, Russia does not have a reefer fleet and only a reduced number of bulkers and oil tankers, while reefer vessels, as well as some oil tankers, now belong to Latvia. Third, the single former USSR fleet has been replaced in the freight market by seven independent national fleets. Fourth, along with the appearance of new national fleets, the management system has undergone a dramatic change from that of the fleet of the former USSR. The transition of the NIS to market economies has equally resulted in the transformation of their State shipping companies to joint stock companies, with the main objective of maximizing profits. Fleet developments in the former USSR and the NIS are summarized in tables 1 and 2.

2. Shipping companies and ports of the NIS used to be natural monopolies in the sea transport of commodities. In the past, these monopolies were reinforced by strict specialization of enterprises with respect to commodities carried and trade routes served. Furthermore, annual and quarterly plans, monthly schedules of sailings, etc., were fixed centrally.

Table 1(a)

Development of the fleet of the former USSR by type, 1985-1991 a/
(Thousand dwt)
(Mid-year figures)

Year	Total	Oil tankers	Bulk carriers	General cargo	Container ships	Others
1985	28 153	7 046	4 758	10 071	638	5 640
1986	28 145	6 255	5 544	9 877	720	5 749
1987	28 556	6 512	5 697	9 831	742	5 774
1988	29 199	6 643	6 157	9 609	799	5 991
1989	29 212	6 192	6 626	10 568	601	5 225
1990	29 360	5 989	6 721	11 225	632	4 793
1991 b/	28 403	5 835	6 162	10 842	645	4 919

Source: *Review of Maritime Transport*, various issues.

a/ Ships of 100 grt and over.

b/ End-year figures.

Table 1(b)

Development of the fleet of the former USSR by flag, as of 1 July 1990 and 31 December 1991 a/
(Thousand dwt)

Year	Total	National flag	Foreign flag
1990	29 267	28 530	737
1991	29 813	27 234	2 579

Source: *Review of Maritime Transport*, various issues.

a/ Ships of 1,000 grt and over.

Table 2(a)

Development of the fleets of NIS by type, 1992-1993 a/
(Thousand dwt)
(End-year figures)

	Year	Total	Oil tankers	Bulk carriers	General cargo	Container ships	Others
Russian Federation	1992	17 235	3 800	3 038	6 456	487	3 454
	1993	17 529	3 886	2 938	6 661	476	3 568
Azerbaijan	1992	489	256	-	95	-	138
	1993	529	286	-	104	-	139
Estonia	1992	701	10	260	315	-	117
	1993	698	10	260	304	-	124
Georgia	1992	-	-	-	-	-	-
	1993	36	-	-	-	-	36
Latvia	1992	1 355	803	-	402	-	150
	1993	1 323	810	-	384	-	129
Lithuania	1992	634	24	160	279	-	170
	1993	595	18	165	250	-	162
Ukraine	1992	6 177	119	2 026	3 272	134	625
	1993	6 206	119	2 022	3 290	131	644
Former USSR b/	1992	1 315	582	428	136	11	158
	1993	1 021	469	366	96	-	90

Source: *Review of Maritime Transport*, various issues.

a/ Ships of 100 grt and over.

b/ Armenia, Belarus, Kazakhstan, Kyrgyzstan, Moldova, Tajikistan, Turkmenistan and Uzbekistan have not confirmed the establishment of registries, and, therefore, a significant number of vessels are reported under "former USSR".

Table 2(b)

Development of fleets of Russia and the Ukraine by flag, 1992-1993 a/
(Thousand dwt)
(End-year figures)

	Year	Total	National flag	Foreign flag
Russian Federation	1992	21 439	16 132	5 307
	1993	21 069	15 941	5 128
Ukraine	1992	6 083	5 818	265
	1993	6 102	5 825	277

Source: *Review of Maritime Transport*, various issues.

a/ Ships of 1,000 grt and over.

3. In the process of economic reforms, the situation has drastically changed, and competition emerged at once:

(i) Among local individual companies for customers:

As centralized planning of cargo carrying by individual companies has been discontinued, they are compelled to compete for cargo. In addition to the former State-owned shipping companies, new shipping enterprises have entered the market. The same applies to many private freight forwarders, agencies and other companies.

(ii) Among local shipping companies for government aid:

This is a new type of competition created by privatization and liberalization. Now shipping companies are striving to obtain government assistance in various forms (subsidies, credits, taxes and other privileges).

(iii) Between local companies engaged in maritime or river shipping:

Over the past few years, maritime shipping companies have been facing competition from river shipping companies using river-sea vessels.

(iv) Between local shipping companies and other shipping companies of NIS and CEE countries

In the past relationships among shipping companies of the countries concerned were regulated at a bilateral level and within the COMECON in such a way that competition did not exist.

(v) Between local and Western shipping companies

Even though this type of competition may already be called traditional, national shipping companies of NIS are confronted with the difficulty of adhering to the business principles observed by their partners. In order to survive in the market, local companies are looking for government decisions which would allow them to use State support without unduly affecting market principles and mechanisms.

4. The general economic changes have resulted in a new operational environment for each of the new national fleets. This is reflected, in particular, in new, unrestricted possibilities of acquiring cargo and in newly emerging relationships

with foreign countries in the field of merchant shipping under free competition, as well as with domestic consumers of shipping services.

B. Measures aimed at fostering competitiveness of NIS national fleets

5. Measures improving competitiveness of NIS national fleets are elaborated and carried out by legislative and executive powers, as well as by their shipping companies.

6. The new situation which the NIS and their fleets are facing has created the necessity to elaborate principles and strategies governing shipping activities. Thus, for instance, the Russian Department of Sea Transport is now preparing "Basic Provisions of State Maritime Transport Policy" which, following approval, will provide the cornerstone of maritime policies.

7. The establishment of national fleets in the former USSR started under extremely difficult conditions at the end of 1991. The fleet has been characterized by drastically reduced reinvestment levels since the early 1980s. As a result, the share of economically and physically obsolete vessels in the fleet rose, the average age of the vessels being more than 15 years. Furthermore, there was a considerable shortage of timber-carriers, bulkers, and small and medium-sized oil tankers, which led to an increasing qualitative gap between tonnage requirements and supply.

8. Given this point of departure, the division of the fleet among the new States calls for the renewal of the fleet without which no increased competitiveness can be expected. Consequently, the States and shipping companies focus their attention on solving this problem. Specific measures taken to resolve it include the Russian Presidential Decree N. 1513, issued on 3 January 1993 on "Measures for Revival of the Merchant Fleet of Russia". In compliance with this Decree, the Ministry of Transport prepared the Programme for the Revival of the Merchant Fleet of Russia for 1993-2000, which was approved by Government Ruling N. 996 on "Realization of Immediate Measures for Revival of the Merchant Fleet of Russia". According to this Ruling, it is intended to supplement the Russian fleet with 589 vessels of 8.4 million dwt, including 422 dry cargo vessels of 4.6 million dwt, 118 liquid cargo vessels of 3.3 million dwt, and passenger and other vessels. At present, the Programme is being implemented, but has a severe lack of finances to purchase vessels.

9. In order for the NIS national fleets to compete, efforts are needed to improve the efficiency of their operations. Governments pursue various relevant measures, *inter alia*, legislation permitting shipping companies to become independent business firms. For this purpose in Russia, for instance, the law "On Enterprise and Owner's Activities", and the Presidential Decree N. 721 "On Transformation of State Enterprises into Joint Stock Companies of an Open Type" have been adopted. Today, all the main shipping companies are joint stock companies and State executive organs have no right to intervene in their operations, i.e. these shipping companies are independent in planning and carrying out their activities, while, at the same time, having some government support.

10. Fleet efficiency is influenced by port efficiency. Consequently, measures are being taken to improve port operations. After the disintegration of the USSR, there was a considerable shortage of port capacities in Russia, which has adversely affected the handling of vessels and, consequently, fleet efficiency. In order to overcome this problem, the Russian Government has approved the Programme of Developing Ports of Russia, under which 22 terminals are being constructed in seaports, which will reduce the transit time in ports, increase the fleet's carrying capacity and improve the quality of shipping services.

11. With a view to improve the conditions for national fleets' operations, NIS countries aim to prepare and conclude various shipping agreements. Thus, for instance, between 1992 and 1994, Russia signed bilateral shipping agreements with Cuba, Viet Nam, China and Lithuania. Similar agreements with Latvia, Estonia and the Ukraine are nearing completion. Furthermore, a multilateral

intergovernmental Agreement on Merchant Shipping in the Caspian Sea is envisaged. Efforts are under way in Russia to ensure participation in the Paris and Tokyo Memoranda, which is expected to have a positive effect for Russian vessels calling at foreign ports.

12. It is common knowledge that safety of navigation affects the competitiveness of fleets. Along with the implementation of fleet renewal programmes, countries take measures to improve the system of State supervision of safety of navigation. Thus, in 1994, Russia put into force the International Management Code for the Safe Operation of Ships and Pollution Prevention, prepared a draft of a new Code of Merchant Shipping and introduced licensing and certification, which will improve the system of State supervision of safety of navigation.

Measures taken at the level of shipping companies

13. Principal activities by shipping companies to improve the competitiveness of their fleets include renewing the fleet, improving operational procedures and upgrading the qualifications of seagoing personnel.

(a) Renewing the fleet

14. In order to renew their fleets, shipping companies implement a set of measures for attracting investments in newbuildings. They look for both domestic and foreign investors, study overseas practices of investing (introducing some of them) and take advantage of the favourable terms for buying vessels in the international market. In implementing investment programmes, Russian shipping companies have signed newbuilding contracts for 76 vessels of 1.3 million dwt funded through a combination of equity and loan financing from both Russian and foreign sources.

(b) Improving fleet operations

15. In order to become more market oriented, shipping companies introduce new management techniques and take measures aimed at improving their operating systems. In this context, shipping companies study more actively the international freight market, pay more attention to shippers' requirements, foster commercial orientation and introduce marketing services. They develop cooperation with foreign companies, individually choose agents and establish joint ventures.

16. Shipping companies also try to find common interests and to formulate a harmonized approach to maritime transport policy. In order to do so, Russian companies have set up various unions and associations, in particular the Union of Russian Shipowners (for former State companies) and the Association of Independent Shipowners (for new private enterprises).

17. All these measures are designed to promote a positive image of shipping companies as reliable business partners in the freight market and, consequently, raise the probability of success in a competitive environment.

(c) Upgrading the qualifications of seagoing personnel

18. There are both governmental and private programmes exist that aim at improving the qualifications of seagoing personnel. In Russia, the public sector provides for three higher State maritime academies (over 12,000 students in 1994) and six secondary establishments - two schools and four colleges (over 3,000 students). Between 1992 and 1994, 3,210 students graduated from higher government maritime academies and 2,100 from secondary maritime educational establishments.

19. In addition to compulsory attendance at maritime training institutions (either in their own countries or abroad), seagoing personnel benefit from various on-board training programmes offered by shipping companies. These companies organize temporary work abroad for their personnel, attend various

domestic seminars, in which foreign experts participate, and also overseas seminars, and participate in domestic and overseas conferences where shipping issues are discussed.

20. These companies also participate in improving the training of future seamen in State educational establishments. An example is their cooperation in introducing professional psychological selection procedures for entry into maritime educational establishments.

Chapter II

PRIVATIZATION OF SHIPPING AND PORT OPERATIONS

A. Principles of privatization and implementation policies

21. A problem which NIS countries have is the privatization of their shipping companies and ports. It has become an important component of privatizing State and municipal property with a view to deepening economic reforms and promoting the development of a market economy.[1]

22. Privatization of State and municipal enterprises in the field of shipping and ports involves, in the countries concerned, the transfer of public facilities, such as ports and port installations, and shipping companies, including ships and other tangible or intangible assets, to the private sector. This is a complex process and may entail several phases, including:

- restructuring, i.e. splitting large public-sector enterprises;
- liquidation and subsequent sale of sellable assets, in particular vessels;
- commercialization or corporatization, i.e. the conversion of public enterprises into corporations under company law, whereby the Government may retain 100 per cent of the shares or where the corporation is partly privatized;
- divestiture, including the option of management or employee buy-outs.

23. The scope, pace, procedure and methods of privatization differ from country to country depending on, *inter alia*, political, economic and other country characteristics, the size of the fleets and the role of ports in the national economy.

24. For purposes of establishing the feasibility of privatizing sea-transport enterprises which are owned by the State or by municipalities, they may be differentiated between:

(i) State enterprises, the privatization of which has been generally forbidden or may only be carried out pursuant to specific decisions of the Government or a government agency especially established for managing State property, taking into account the views of competent ministries; enterprises providing certain essential services, generally available to the shipping industry or to the community as a whole, may fall under this category, such as hydrographic and ice-breaking services, environmental control services, vessel traffic systems, etc.

(ii) Enterprises and objects of State and municipal property which are subject to privatization on decisions of the Government or the subordinate administrative entity of a given country (territories or districts, as well as some large port cities, etc.); shipping and port and terminal operating companies fall under this category.

---

[1] The necessity for and general principles of privatization have been extensively dealt with by UNCTAD in the context of the Ad Hoc Working Group on Comparative Experiences with Privatization. Consequently, this chapter only deals with specific aspects of privatizing shipping companies and ports in NIS countries. For a general discussion on the objectives, policies and state of affairs with regard to privatization, see, *inter alia*, UNCTAD "Design, implementation and results of privatization programmes: a cross-country review of national experiences" (TD/B/WG.3/7/Rev.2), Geneva, 1994; and Im, S., Jalali, R. and Saghir, J. "Privatization in the Republics of the Former Soviet Union: Framework and Initial Results", The World Bank, June 1993.

25. In the process of determining policies of privatization and corresponding implementation measures, the following options may be considered:

- Enterprise reform, including restructuring (organizational, financial and operational) and corporatization. In this case, no transfer of ownership takes place, i.e. the enterprise remains in the public sector but it is managed on a commercial basis.

- Partial divestiture, whereby the State retains partial ownership and certain rights in the management of the enterprise, such as protection against hostile take-overs, maintenance of socially desirable activities, etc.

- Privatization without restriction.

Methods of privatization cover mainly:

(i) sale-purchase transactions at auctions;

(ii) selling State shares in an enterprise's capital after its transformation into a joint stock company;

(iii) leasing enterprise property.

26. Table 3 lists privatization options available to Russian ports and shipping enterprises. The main difference between these options relates to the degree of personnel involvement in the ownership of newly privatized companies, and thus to the mechanisms employed to cushion possible adverse social impacts of the privatization process.

Table 3

Privatization options available to ocean carriers and ports in the Russian Federation

Option	Preferential shares given to personnel	Common shares sold to personnel (%)	Common shares sold to management (%)	Common shares available for sale to public a/ (%)
Option 1	Fixed share	0-10	1-5	up to 75
Option 2	-	0-51	-	49-100
Option 3	-	0-20	20	60-80

a/ Including shares retained by the State or the public sector.

27. The options are the following. According to option 1, the personnel receives free-of-charge preference (non-voting) shares constituting a fixed portion (for example, 25 per cent) of the nominal capital, but no more than a 20-fold amount of a minimum monthly pay per worker set by the law. Ordinary shares of up to 10 per cent of the nominal capital, but no more than a 6-fold amount of a minimum monthly pay per worker set by the law are sold to the personnel at a discount (for instance, 30 per cent off their par value) and against a deferred payment (for example, up to three months). The initial instalment may generally not be less than 50 per cent of the share value. The management of an enterprise being privatized has the right to buy up to 5 per cent of ordinary shares at their par value. This option was chosen in Russia, for example, by companies such as the Novorossiysk Shipping Company and the Northern Shipping Company, as well as the Vostochny Sea Commercial Port, the

Kholmsk Sea Commercial Port, the Vanino Sea Commercial Port and the Anadir Sea Commercial Port.

28. In the Novorossiysk Shipping Company, the personnel has a share package of 49.7 per cent: 45 per cent belong to the State and 5.3 per cent are for sale to the public in a free market; in the Northern Shipping Company, the respective figures are 45 per cent, 20 per cent and 35 per cent; and in the Vostochny Sea Commercial Port, the figures are 44.8 per cent, 20 per cent and 35.2 per cent.

29. Under the second option, the personnel of the enterprise being privatized have the right to acquire ordinary (voting) shares up to 51 per cent of the nominal capital. In this case, an allotment of shares free of charge and their sale on privileged terms are not practised. This option is used in Russia by joint stock companies such as the Far Eastern Shipping Company (51 per cent of the shares belong to personnel, 20 per cent to the State and 29 per cent are sold to the public), the Murmansk Shipping Company (51 per cent and 49 per cent; no shares are intended for sale) and the Kamchatsk Shipping Company (49 per cent and 51 per cent; no shares are for sale).

30. In addition, option 2 is used by port joint stock companies, such as the Novorossiysk Sea Commercial Port, the Sea Commercial Port of St. Petersburg, the Vladivostock Sea Commercial Port, Arkhangelsk Sea Commercial Port, the Tuapse Commercial Port, the Krasnogorsk Sea Commercial Port, as well as the Korsakov Sea Commercial Port, the Nakhodka Sea Commercial Port and the Commercial Port of Posjet. In the first six cases, the distribution of shares is 51 per cent, 20 and 29 per cent, and in the last three cases, 51 and 49 per cent (no shares for the public); 61 per cent, 28.54 and 10.46 per cent; and 51 and 49 per cent (no shares for the public).

31. Option 3 has not been used yet by shipping companies or by ports. Under this option, the personnel of the enterprise may buy ordinary shares up to 20 per cent of the nominal capital but no more than 20-fold the amount of a legally fixed minimum monthly pay per worker, with a discount of 30 per cent off their par value and a deferred payment for three months. The amount of the first instalment may not be less than 25 per cent of the share par value.

32. The choice of option is taken by the general meeting of the personnel. It is considered valid if no less than two thirds of the enterprise personnel on the payroll vote for it. In the absence of a two-thirds majority, the first option is applied.

33. It is important that shares acquired or received free of charge may be sold by shareholders without any restrictions.

B. Some examples of the state of privatization in NIS

(i) Shipping

34. The speed and extent of privatization of maritime sector enterprises differ considerably among the various NIS countries. The Baltic Republics, for instance, have three major shipping companies (Latvian Shipping Company, Estonian Shipping Company and Lithuanian Shipping Company). They are independent but still State-owned, although the countries stressed their wish to convert them into joint stock companies. It seems that this action, as well as privatization, will not take place very soon.

35. In the Ukraine, a joint stock shipping company, Blasco, has been created by Presidential Decree on the basis of the former Black Sea Shipping Company.

36. It is also noteworthy that, in Russia, vessels belonging to various organizations and enterprises, including those being privatized, are sold at auctions. Part of the revenue (30 per cent) goes to a relevant organization or an enterprise and the remaining 70 per cent goes to State organs of privatization and is used for financing the privatization process.

(ii) Ports

37. With respect to seaports, their privatization, judging by Russian practices, is carried out in three phases. In the first phase, ports are turned into joint stock companies. However, given their strategic importance, a considerable part of the property remains in State ownership. Privatizable assets of ports do not include port infrastructure (berths, breakwaters, canals, lighthouses, navigation aids, rail tracks and access roads) or objects related to port supervision, pilotage, vessel control systems, environment protection, labour protection and other non-commercial services.

38. In the second phase, the port joint stock company is reorganized. Operational, commercial and technical activities and services are commercialized, and subsequently the activities concerned are opened to competing enterprises (stevedores, terminal operators, ship chandlers, freight forwarders, agencies and others). These companies may use the port infrastructure under long-term lease arrangements and may buy privatized superstructures and equipment.

39. In the third phase, a State enterprise is established in the port to provide services not subject to privatization and to perform sovereign functions.

40. Russian ports are administered by the Maritime Administration of the Port (MAP). The main task of the MAP consists of ensuring safety of navigation and order in the port, including supervision of fulfilment of laws, regulations and international agreements on merchant shipping, supervision of technical operations and development of port structures and services and properties not subject to privatization and allotted to it. MAP operations, as well as repair, development and building of port infra- and superstructures, are funded through income generated from port dues, lease of State property and various services related to the fulfilment of the MAP functions.

41. In the Baltic Republics, all the ports are either State or municipal property and their privatization is not on the agenda. The port of Klaipeda (Lithuania) is not subject to privatization.

42. A number of issues remain to be resolved regarding the privatization of seaports. First, the division of the once single-port organism into two parts (privatized and non-privatized) and the further split of privatized activities into various companies holds the danger of unlinking port units and complicating their management. This is fraught with the diminishing interest of both sides in investing in new port installations. Second, the present approach to port privatization may not contribute to increasing competition, as in many cases it would hardly be possible for newcomers to compete with existing companies that have storage space and handling equipment. As a matter of fact, competition is most likely to develop in agency, ship-chandling and freight-forwarding operations.

43. Therefore, the option of privatization, in which all port property is transferred to a joint stock company, may also seem to deserve attention in some cases. Then it is included in the nominal capital of the joint stock company which, within a certain period, pays for it and becomes its owner. The State would continue to be the owner of the land on which the port is situated and of the water area and would receive rent from the joint stock company. The main advantage of this option is that it does not imply the division of the port into individual, independent parts.

C. Social impact of privatization

44. Privatization may entail some negative consequences for the position of employees, such as the reorganization of an enterprise and even its closure, job losses, etc. Therefore, in Russia, with a view to protecting the interests of the personnel of the enterprises being privatized, it may be forbidden, for a specified period of time, to reorganize, liquidate or modify the enterprise structure without the consent of competent authorities, or to make changes in

the enterprise personnel or reduce its number, without the approval of the personnel, or of an organ authorized by the personnel.

D. Legal and institutional framework of privatization

45. The process of privatization of shipping and port operating companies is, of course, an integral part of the national and/or regional and/or industry-wide programmes of privatization of any of the successor States of the former Soviet Union. Relevant laws and institutions exist or are about to be enacted in some of the NIS, including Russia. Thus, privatization in Russia is largely regulated by the laws on "Enterprises and Owners' Activities" (1990), "Privatization of State and Municipal Enterprises in the Russian Federation" (1991), the Presidential Decree on "Organizational Measures for Transforming State Enterprises, Voluntary Associations of State Enterprises into Joint Stock Companies" (1992, N 721), and the "State Programme of Privatization of State and Municipal Enterprises in the Russian Federation" (1994) providing, *inter alia*, for privatization of maritime transport enterprises.

46. Privatization of State property is organized by privatization agencies. In Russia, it is the "State Committee for Managing State Property (Goscomimuschestvo)" which has territorial agencies and is financed from the State budget.

47. Public corporations, as well as State shares in the capital of enterprises, are sold only by the Russian Fund of Federal Property and its representatives. The Fund is financed by resources gained from the privatization of State enterprises. It has local divisions. The Fund promotes joint stock companies but, in principle, has no right to intervene in the enterprises' activities. On the other hand, it is important that the Fund maintain close relationships with government and administrative entities at all levels that determine privatization policies and the regulatory framework within which privatization can take place. In this context, it is important to mention agencies or ministries in charge of formulating and implementing competition policies in order to back up properly the privatization of ports, in particular those that may be considered as natural monopolies.

48. Success or failure of privatization in the NIS largely depends on the availability of a functioning financial market that ensures sale and purchase of shares and the institutional framework relating thereto. This market, however, has not yet been developed in all countries of the former USSR. This lack is particularly felt in the implementation of policies of sales of shares to the public. There are also, however, other, more general conditions for successful privatization efforts. These include:

- governments' firm political commitment to privatization;
- clarifying solutions to conflicting political, economic and social objectives;
- building a broad-based consensus among all parties, including users of port and shipping services;
- elaborating instruments that foster competition;
- promoting private-sector development;
- creating a stable political, economic and social environment conducive to private investment in the maritime sector of the NIS.

49. While privatization in the field of shipping and ports has made some progress, it is still too early to assess comprehensively its impact on national shipping and trade. In the process of privatization, the old system of management and control is being destroyed and favourable conditions for fostering the efficiency and competitiveness of shipping companies and ports are being developed. However, at the same time, government supervision of safety of navigation, technical conditions of vessels and marine structures may not always be adequately assured.

Chapter III

LIBERALIZATION OF SHIPPING MARKETS

A. General considerations

50. The national shipping policies of the former socialist countries of Eastern Europe were, to some extent, characterized by contradictions with international shipping policy. This was apparent, first of all, with respect to market access. Socialist countries pursued a policy of restricting access of foreign shipping service providers to their overseas cargo. The unavailability of free-market access and competition resulted in a substantial development of their national fleets and in very high shares in the transport of national foreign-trade cargo.

51. At the same time, when an opportunity arose, the countries concerned declared their adherence to the principles of free market, equality, non-discrimination and mutual benefit. These were reflected in the overwhelming majority of their shipping agreements and conventions concluded at various international forums. Thus, the Agreement on Cooperation in Merchant Shipping, which was signed by the heads of Ministries responsible for the maritime fleets of Bulgaria, Hungary, the former German Democratic Republic, Poland, Romania, the former USSR and the former Czechoslovakia, and which entered into force in 1973, stressed, in particular, that the parties to the Agreement confirm their adherence to the principles of freedom of the maritime navigation and their determination to oppose any discriminatory measures in that field that could damage the normal progress in the development of shipping (article 3).[2]

52. The shipping policy of the countries concerned was thus characterized by a split approach under which national markets were in fact closed, while at the same time opportunities offered as third-flag carriers in other countries' trades were systematically exploited. The consequent pursuit of unilateral advantages for national fleets through alleged adherence to internationally accepted concepts and practices had often resulted in conflicts with trading partners and hindered the development of true cooperation in international shipping that was for the benefit of all countries.

53. After the breakup of the USSR, NIS and CEE countries, which assumed the way of developing a market economy, have been faced with the problem of changing the essence of their national shipping policies. The initial fundamental principle of the new policy is transition to the concept of free access to shipping markets. This implies the participation of national fleets in international shipping on the basis of a free market, fair competition and equality among market players.

54. The set of common shipping policy principles to be observed has been explicitly stated during consultations between members of the OECD Maritime Transport Committee and representatives of NIS and CEE countries. These agreed principles are as follows:[3]

Principle I. The participation under free and fair market competitive conditions of seagoing ships of any nationality in international seaborne trade.

Principle II. Non-discriminatory treatment with respect to access to ports open to international trade, the use of infrastructure and auxiliary maritime services of those ports, as well as related fees and charges.

Principle III. Non-discriminatory treatment as regards agency operations and relations with forwarders.

---

[2] "Experience of member countries of the Council for Mutual Economic Assistance in developing cooperation in the field of maritime transport" (UNCTAD/SHIP/625), annex I.

[3] See OECD Press Release, SG/PRESS(93)37, Paris, 10 June 1993.

Principle IV. The freedom for shipping companies to offer an efficient total transport system (multimodal transport services) and engage in joint venture investments.

Principle V. The free, efficient and timely transfer of funds related to all aspects of commercial shipping operations.

Principle VI. Encouragement of cooperation through commercial negotiations between shipping companies while adhering to the principles of free and fair market commercial operations.

Principle VII. Adherence to market pricing practices by all parties involved in commercial shipping operations.

Principle VIII. Freedom for shippers to choose among different shipping service for the transport of commercial cargoes on all trade routes.

Principle IX. Open access to inland waterways for all seagoing vessels engaged in the maritime-related transport of commercial cargoes in international trade.

Principle X. Compliance with applicable international rules and standards regarding maritime safety and training, the prevention of pollution of the environment and the living and working conditions on board vessels.

Principle XI. Improvement of transparency as regards those involved in maritime transport operations.

Principle XII. Consultations: Parties to this Understanding, while not inhibiting bilateral discussions of Parties involved, agree to consult as regularly as needed.

55. The formulation of new shipping policy principles and the firm intention to implement them imply the acceptance of new conditions under which shipping business is being conducted, in particular, the rejection of the old principle of priority and uncompetitive access by domestic fleets to national cargo flows. Liberalization of international maritime shipping and freedom of market access have become cornerstones of new policy directions.

B. Policy instruments affecting market access

(i) Cabotage restrictions

56. In Russia, carriage and towage between national ports situated on the same sea (small cabotage)[4] and between national ports situated on different seas (great cabotage) shall be restricted to ships flying the flag of the Russian Federation. Exceptions to this rule may be established by the Russian Government.

(ii) Restriction on access of foreign vessels to inland waterways

57. Vessels flying a foreign flag may be restricted to enter inland waterways. Thus, in Russia, according to the Charter of Inland Waterways, this is a rule with two exemptions. The first exemption concerns vessels belonging to diplomatic and consular representations in compliance with existing international agreements and customs. The second applies to vessels under the flags of Azerbaijan, Kazakhstan and Turkmenistan, which have been granted access to inland waterways in Russia since July 1994.

58. The list of rivers, the mouths of which are open to seagoing vessels flying foreign flags, is set by competent government agencies.

---

[4] For the purpose of cabotage, the following are considered as one sea: (a) the Black Sea and the Sea of Azov; (b) the White Sea and the Arctic Ocean; (c) the Sea of Japan, the Sea of Okhotsk and the Bering Sea.

59. This restriction seems to be outdated and may be further relaxed or fully removed. A significant step in this direction is the Partnership and Cooperation Agreement between the European Community and its member States, and the Russian Federation, signed on 24 June 1994. The Parties concerned agree that no later than 31 December 1996 they will conduct negotiations on the stage-by-stage opening of the inland waterways of each Party to the nationals and shipping companies of the other Party, in respect of the freedom to provide international sea-river services (article 39, paragraph 3).

(iii) Restriction on calling at certain ports

60. The opening of ports to foreign vessels is a major prerequisite for free market access. There remain, however, cases of restrictions of port access, i.e. foreign vessels are not allowed to call at certain ports. The number of closed ports is decreasing and, consequently, their role is diminishing. Thus, in Russia, between 1992 and 1994, 14 closed ports became open to foreign vessels, i.e. Vladivostock, Khasanskiy, Beringovskiy, Gelendjik, Posjet, Makhachkala, Korsakov, Magadan, Nikolaev-on-Amur, Anapa, Petropavlovsk-Kamchatskiy, Sovetskaya Gavan, Slavyanka and Astrakhan. No doubt, these ports will remain open and, in the future, national and foreign vessels will have the possibility to call at the same ports with some rare exceptions.

(iv) Cargo reservation

61. A number of the countries in transition to market economies are parties to the United Nations Convention on a Code of Conduct for Liner Conferences.[5] According to the Convention, the group of shipping lines of each of two countries, the foreign trade between which is carried by the relevant liner conference, shall have equal rights to participate in the freight and volume of traffic generated by their mutual foreign trade and carried by the conference. Third-country shipping lines shall have the right to acquire a significant part, such as 20 per cent, in the freight and volume of traffic generated by that trade.

62. In this light, it is pertinent to refer to the above-mentioned Partnership and Cooperation Agreement[6] establishing a partnership between the European Community and its member States, and the Russian Federation. The Agreement stipulates that, with regard to maritime transport, the Parties undertake to apply effectively the principle of unrestricted access to the international market and traffic on a commercial basis, a provision that is considered not to prejudice the rights and obligations of the Parties arising under the United Nations Convention on a Code of Conduct for Liner Conferences.

63. The Parties affirm their commitment to a freely competitive environment as being an essential feature of the dry and liquid bulk trade (article 39, paragraph 1(b)). In applying these principles, the Parties shall not use, in their mutual trades, as from entry into force of the Agreement, any cargo-sharing provisions of bilateral agreements between any member State and the former Soviet Union, nor shall they introduce cargo-sharing arrangements in future bilateral agreements with third countries concerning dry and liquid bulk and liner trade (article 39, paragraph 2(a), (b)).

(v) Movement of labour

64. Measures prohibiting or restricting the international movement of seamen can also be observed. Thus, in Russia, the members of the crew must be nationals of the country. Exemptions to this rule may be permitted in accordance with established government procedures. It appears that the reduction of tonnage and the consequent redundancy of seagoing personnel are among the main reasons for prohibiting or restricting foreign crews for some time.

---

[5] CEE countries: Bulgaria, Czech Republic, Romania, Slovakia
NIS countries: Russian Federation.

[6] See para. 59 above.

C. Price-based measures aimed at promoting domestic providers of shipping services

(i) Subsidies

65. Before privatization and liberalization began, the USSR Government provided investment and operating subsidies to the State-owned shipping companies. The amount of government investments *vis-à-vis* investments from revenues of these Russian companies is given in table 4.

Table 4

Investments in the Russian shipping industry
(In million roubles, constant prices of 1991)

State-owned shipping companies	Centralized (government) investments 1986-1991	Investments from revenues of the shipping companies 1986-1991
Northern Shipping Company	64.26	1 015.72
Murmansk Shipping Company	108.23	442.43
Baltic Shipping Company	122.98	1 683.57
Novorossiysk Shipping Company	60.50	1 564.56
Far Eastern Shipping Company	385.51	2 423.83
Sakhalin Shipping Company	54.94	630.77
Kamchatka Shipping Company	37.78	232.86
Primorsk Shipping Company	39.80	381.88
Arctic Shipping Company	11.06	117.87
TOTAL	885.06	8 493.49

66. Today, for financing the Programme of Revival of the Merchant Marine of Russia, a special fund has been established which provides for a government share of investments. Resources of the fund are available to enterprises on condition that no less than 80 per cent of investments are covered from their own revenue, i.e. the government share constitutes up to 20 per cent. This subsidy is mainly aimed at developing a national shipping industry and is consequently not available to foreign providers of shipping services.

(ii) Tariffs and charges

67. Freight rates and charges for shipping services are still regulated to a certain extent by the State. It applies to cabotage shipping where tariffs have not been liberalized, as well as to port dues and charges. Dues and charges may be an impediment to market access by foreign shipping companies. Thus, a general rule is that national vessels in foreign traffic and foreign vessels flying the flags of the States with which a relevant NIS country has agreements that stipulate the national treatment or the most-favoured-nation treatment pay the same dues and charges. Another scale of port dues and charges is applied to all foreign vessels flying the flags of the States with which a relevant country has no agreements mentioned previously. Such vessels' dues and charges may be several times higher than those of the first group of vessels.

68. Tariffs for international shipping are now liberalized and market freight rates are quoted. With the view to further liberalization, cabotage and port tariffs are soon expected to be freely quoted.

D. Relaxation of government intervention

69. Along with the introduction of international shipping-policy reform, some countries have started formulating new relations within their national domestic maritime transport complexes (NMTCs).[7] The organizational structure of the NMTC may include a relevant government agency (a transport ministry with a sea-transport department or a maritime transport ministry or a separate sea-transport department, etc.), associations of national shipowners, organizations and companies dealing with chartering vessels, brokerage, bunkering, communications, data processing, dissemination of information, research, educational and training establishments.

70. In the Ukraine, for example, the government agency dealing with transport is the Ministry of Transport. To improve the Ukrainian maritime transport management, the State Administration for Maritime Transport of the Ukraine (UKRMORFLOT) has been set up. It is independent and does not constitute a part of the ministerial structure. The main tasks of the Administration include:

- formulation and implementation of policy measures aimed at an economically justifiable utilization of the merchant marine for transport of commodities and passengers in overseas shipping and cabotage, as well as the development of cross-trade shipping;

- improving safety of navigation;

- regulation of merchant shipping.

71. The Administration has 10 departments which, in turn, are divided into divisions responsible for various matters of maritime transport activities. It exercises control over the Registry, the Azov, the Black Sea and the Ukrainian Danube shipping companies, as well as ports and ship-repair yards. It is responsible for safety of navigation and supervises scientific research organizations.

72. A major prerequisite for new relations in the maritime transport sector is the enactment of laws and regulations. These have enabled enterprises to be privatized or commercialized, have promoted a change in relations between shipping companies and government agencies and have created a framework for commercially oriented operations of the shipping industry. Only a few years ago, a system of centralized planning and management prevailed in these countries. The only form of ownership in national economies, including shipping, was State ownership, and the major source of investments in merchant shipping was capital expenditures from the State budget. The bureaucratic hierarchy of management (the State Planning Committee, ministries, etc.) took resources for investments from the budget and distributed them. Of course, enterprises had their own funds for developing production but that did not modify the system. In those circumstances, the principal criteria by which the efficiency of investments was assessed were State interests and the State did the utmost to protect them. Under the new conditions, government agencies have lost the power of direct

---

[7] This complex denotes enterprises, associations of enterprises, institutions and organizations, regardless of ownership engaged in sea transport, freight forwarding, repair and technical exploitation of vessels and their equipment, research, design and marine project implementation, training and other activities related to maritime navigation. In 1993, the NMTC of Russia numbered 110 major enterprises and organizations, including 10 shipping companies (formerly State-owned), 40 ports, 13 ship-repair yards, 3 State higher educational academies, as well as 250 auxiliary enterprises. The value of capital assets was over 500 billion roubles and the number of employees was 154,000.

management and control of companies. Their functions are now limited to those of government regulation and coordination.

73. The new concept of governing (not managing or operating) maritime transport has created conditions for liberalizing the national shipping industries of the NIS countries. The appearance of joint stock companies and privatization has contributed further to decentralization and deregulation. Government interference in activities of enterprises is now limited to developing favourable conditions for efficient operations of maritime transport enterprises.

74. A general relaxation of government control over the national maritime transport complexes, based on the general conditions of transition to a market economy, has resulted in new mechanisms for liberalizing shipping of NIS countries. Among these mechanisms there are mainly:

- development of direct business links by enterprises;
- introduction of new elements in investment policy;
- establishment and fostering a competitive environment;
- freedom to work on board foreign vessels; and
- public mechanism of liberalization, protection of interests and coordination of national shipping companies' activities.

(i) Development of direct business links by enterprises

75. In former socialist countries, the system of directive planning governed the maritime sector, i.e. all the interaction of maritime transport enterprises among themselves, with customers or other modes of transport, was carried out centrally through competent government agencies. After the collapse of the former Soviet Union and transition of the countries to market economies, enterprises were given the right to establish business links independently. Permission to develop direct links has fostered the development of commercial activities of the companies. It has widened, in particular, the possibilities of canvassing cargo. A positive factor of the mechanism is also the closer contact between providers and users of shipping services, which allows shipping companies to implement more effectively marketing policies and to meet users' requirements.

(ii) Introduction of new elements in investment policy

(a) Reduction of government investments

76. A feature of investment policy in national shipping of the countries concerned is, among other things, a dramatic reduction in government investments. The main burden of investments is now with the shipping companies. However, enterprises do not have enough of their own resources and are forced to seek capital actively. Therefore, efforts to attract domestic and foreign investors are greatly increased and a full replacement of the previous investment mechanism becomes urgent, involving, first of all, diversification of investment sources.

77. To facilitate the solution of this task, countries have adopted a number of legal documents.*

(b) New and increasing efforts to attract foreign investments

78. A fundamental task of NIS and CEE countries is to attract and efficiently use foreign financial resources, advanced technologies and management experience in the national economies, including the shipping sector. To cope with this need, a set of measures constituting an essential part of the new investment policy is being considered. It includes policies related to the attraction of foreign investments, conclusion of concession agreements, establishment of free economic zones, preparation of comprehensive programmes for stimulating foreign

---

* In Russia, the law "On Foreign Investments in the Russian Federation" (4.07.1991) and the Government's Ruling "On Making More Active Efforts to Attract Foreign Investments to the Economy of the Russian Federation" (29.04.1994).

investments and conclusion of agreements with foreign countries on reciprocal protection and encouragement of investments. It is obvious that these and other measures to promote foreign investments have a direct impact on the ability to attract foreign capital to the maritime sector.

79. Government investment policies and mechanisms cover the most crucial points of providing incentives for foreign investments. Foreign investors are considered to be mainly foreign juridical entities, i.e. companies, enterprises, organizations, associations, etc., as well as foreign natural persons, foreign States and international organizations. In principle, they have the right to make investments in the territories of the NIS countries by:

- a share participation in enterprises established jointly with juridical persons and citizens of the NIS countries concerned;
- establishing enterprises wholly owned by foreign investors as well as affiliates of foreign juridical persons;
- acquisition of existing domestic enterprises, buildings, structures, shares, obligations and other property which, in compliance with existing national laws, may be owned by foreign investors;
- acquisition of rights to use land and other natural resources;
- acquisition of other property rights;
- other activities relating to investments that are not prohibited by national legislation, including the granting of loans, credits.

80. Foreign capital may be invested in any objects not prohibited by national laws, including in new and modernized capital and current assets of the shipping industry. Foreign investments also enjoy full and unconditional legal protection awarded by national laws and regulations as well as international treaties valid in the territories of the countries. Legal treatment of foreign investments and activities of foreign investors related to investments may not be less favourable than the treatment afforded to nationals.

81. An important aspect is that foreign investments are guaranteed against the compulsory withdrawal of governments. According to legal acts, foreign investments may not be nationalized and are not subject to requisition or confiscation except in exclusive situations stipulated by national laws when this is permitted and in the public interest. In cases of nationalization or requisition, foreign investors shall be paid an adequate and prompt compensation.

82. Foreign investors may, without restrictions, transfer abroad their revenue relating to their investments, if this revenue is received in foreign currency. Thus, according to the USSR-Germany Agreement on Shipping of 1991 (article 15), either of the Contracting Parties shall grant to maritime shipping enterprises of the other party the right to transfer revenue abroad in freely convertible currency.

- Promotion of joint ventures

83. Liberalization of the NIS and CEE countries' shipping enables the interests of shipping enterprises to be linked. As a result, there are now numerous joint ventures with a share of foreign capital.[9] The use of joint ventures helps to obtain additional resources for the renovation of national fleets and amplifying capacities of sea ports, to raise loading rights and increase profits.

84. The matter of joint ventures is reflected in national and international documents, for instance, in bilateral shipping agreements. Thus, in compliance

---

[9] Of the CEE countries, Poland serves as an example. The national line "POL" has had considerable experience with regard to cooperative arrangements. It has concluded joint ventures with Danish and German capital (respectively "Frank and Toliesen Poland Ltd., Shipping and Forwarding" and "POL Supply Ltd."). Interests of "POL" in joint ventures cover not only maritime transport but also inland haulage, freight forwarding, brokerage, warehouse operations, ship-chandling, etc. All in all, "POL" has shares in more than 30 national and foreign companies.

with the USSR-Germany Shipping Agreement (article 7), both parties to the Agreement shall render assistance to shipping or shipping-related and commercial entities of the other party in establishing a shipping line to/from ports of the other party, as well as in establishing representations or joint ventures on the territory of the other party.

- Fostering foreign investors' participation in privatization

85. As mentioned, foreign investors may take part in domestic privatization. They are allowed to share privatization of State and municipal enterprises, as well as objects of unfinished capital construction. Terms of their participation in privatization tenders and auctions are determined by respective national acts. The cost of privatized property is covered in national or foreign currency.

(iii) Regulatory framework for establishing and fostering a competitive environment

86. A most important component of economic reforms in NIS countries is the establishment and fostering of a competitive environment in shipping markets. In practical terms, competition originates mainly from converting formerly State-owned companies into joint stock companies and their commercialization and subsequent privatization, together with the promotion of further private-sector participation in these shipping markets.

87. In their efforts to ensure and enhance competition, the countries concerned determine regulatory frameworks for preventing, restricting and banning monopolistic activities and unfair competition, and set conditions for the establishment and efficient functioning of shipping markets. They prohibit a company from enjoying a dominant position which may result in a restriction of competition and/or abuse of power to the detriment of other companies or nationals. They also partly or fully prohibit agreements (coordinated activities) of competing companies (potential competitors) having together a dominant position, if such agreements (coordinated activities) result or may result in a considerable restriction of competition.

88. With the aim of developing markets and competition, there may be in principle privileged credits, reduced taxes or tax-relief measures for "infant" companies, policy instruments concerning the attraction of foreign investments, the establishment of joint ventures, the introduction of changes in types of activities to be licensed, etc.

89. Particular importance should be given to small private companies that have recently appeared and that start affecting shipping services markets.

90. The sector is regulated by merchant shipping codes and other regulatory mechanisms, including a set of licensing measures. The concept of licensing is reflected, for example, by the Russian Government's Ruling "On Licensing Transport, Transport Freight Forwarding, Broking and Other Activities Related to Carrying out the Transport Process by Maritime and Inland Water Transport in the Russian Federation" (23.08.1993, N 840). This concept implies using licenses not only as a means of prohibiting or restricting market access, but also as an instrument to regulate maritime transport under market relations.

91. Regulatory documents on licensing also provide, in some cases, for a universal and simple system of levying licence fees depending on revenues of activities to be licensed. In order to protect the interests of enterprises applying for licenses, an independent maritime licence examination is given.

(iv) Freedom to work on board foreign vessels

92. In the process of economic reforms in national shipping, some countries began to grant the right to their nationals to enter the international labour market and to work on board foreign vessels. Given their qualifications and low wages, these seamen are in demand and their availability will increase competition in the international labour market of seamen.

(v) Coordination of national shipping companies' activities

93. With the independence and self-sufficiency of shipping companies of NIS countries, the necessity arose to protect their interests and coordinate their activities. In order to achieve this, shipowners resorted to various forms of cooperative arrangements. They have established, in particular, unions or associations or councils which elaborate common positions and protect their interests at various levels (government agencies, the parliament, other organizations).

E. Other support measures to promote national fleets

94. In addition to the measures described previously, the countries concerned use a variety of support measures aimed at promoting their national fleets.

(i) Measures to improve the employment situation

95. Among other things, the provision of labour is of utmost importance for developing national fleets. Therefore, the States concerned have developed measures to ensure favourable employment conditions for seamen, thus contributing to the successful activities of national fleets. Relevant measures are manifold and, while in most cases are generally applicable to the labour markets, there are others that are specifically applicable to employees of the shipping industry.

96. The general objective of government measures is to ensure the social security of employees, regulated by the Russian federal law "On Collective Treaties and Agreements" (11.03.1992, N 2490-1). According to this law, a sector tariff agreement is concluded between trade unions of water (or sea or river) transport, trade unions of seamen and dockers, employers at maritime transport enterprises and the labour ministry. Such an agreement regulates, at the level of the industry, relationships among the parties in the sphere of labour organization, conditions and pay, employment, hiring and dismissal and social privileges. Conditions generally reflect the conventions and recommendations of the ILO ratified by the countries concerned. The specific purpose of such regulatory measures in the maritime sector is to prevent existing personnel from leaving maritime transport enterprises and to attract new workers, thus providing the national fleets with a constant supply of labour, particularly shipboard labour.

(ii) Investment policy

97. The investment policy of NIS countries is a basic instrument to promote the development of national fleets. The countries determine their investment policies in acts and other regulatory documents which are annually reviewed and, if necessary, corrected. In Russia, the implementation of investment policies is, to a large extent, based on the provision of the Programme for the Revival of the Fleet of Russia for 1993-2000.[19] Furthermore, provisions of public investment will be governed by the necessity to maintain safety of maritime transport though the provision of publicly available services, such as ice-breaking, vessel traffic systems, port infrastructure, etc.

(iii) Promoting overseas cooperation

98. In the course of liberalization of international shipping services of NIS countries, governments are pursuing a policy of international cooperation in shipping which, in turn, contributes to the development of national fleets. Consequently, the establishment of conditions for cooperation with other countries and successful coordination of this cooperation is considered an important government measure to support the countries' national fleets.

99. Government policy instruments for promoting cooperation in international shipping are numerous. One is bilateral shipping agreements. Thus, in 1992-

---

[19] See also para. 8, above.

1994, bilateral shipping agreements were signed between Russia, on the one hand, and Lithuania, Cuba, Viet Nam and China, on the other. Bilateral agreements on shipping between Russia and Latvia, Estonia and the Ukraine are ready for signature, while agreements between Russia, Georgia, Azerbaijan and Turkmenistan are being negotiated. New bilateral shipping agreements between Russia and the United States, France, Greece, Spain, Cyprus, Italy, Algeria, the Republic of Korea, Taiwan Province of China, Israel and Albania, reflecting contemporary changes in shipping, have been agreed at expert level.

100. On the basis of bilateral agreements, mixed maritime commissions are being established. Activities of these commissions are aimed at solving problems contributing to the development of the fleets and their effective operations, clarifying positions in international organizations, etc. The pattern of questions discussed at government level, and the conclusions and discussions, help to create advantageous conditions for fleet development.

101. Cooperation is also provided for countries members of the Commonwealth of Independent States (CIS), which comprise the majority of the republics of the former USSR."

102. Multilateral cooperation is carried out through UNCTAD, the United Nations Economic Commission for Europe (ECE), the European Union (EU), and the Organisation for Economic Co-operation and Development (OECD), etc. Furthermore, Russia, for example, will join the Paris Memorandum and the Tokyo Memorandum, which will have a positive effect for Russian vessels calling at European and Asian ports.

(iv) Coordinated approach to solving transport problems

103. After the CIS was instituted, common transport problems have been solved at government level through the mechanisms provided by a Transport Coordination Meeting. The following problems are being addressed: where to establish the demarcation between Russia and the Ukraine in the Azov sea area and the Kerch strait, and determining the modalities for the use Ukrainian ports by Russian vessels. Given the need for a continuous dialogue, further institutionalization of such interactions would help to arrive at mutually acceptable solutions to common shipping problems, and, consequently, would support the development of national fleets.

F. Participation in international organizations

104. At present, NIS countries protect the interests of their fleets in important organizations, such as IMO, ECE, UNCTAD, the Danube Commission, ILO, etc., that deal with shipping. Thus, the countries concerned take an active part in the activities of international government organizations. These activities reflect close links between the State and its shipowners and strengthen the government's role in supporting interests in national shipping.

" With this purpose in view, the Government of Russia has adopted the special ruling "On Measures for Ensuring the Implementation of the Agreement on Common Conditions and Mechanism of Supporting the Development of Production Cooperation of Enterprises and Industries of States Members of the Commonwealth of Independent States and the Protocol on Mechanism of Realizing this Agreement" (24.10.1994, N 1190).

Chapter IV

IMPACT OF POLICY REFORM MEASURES

105. In the following pages, some preliminary assessments of the impact policy reforms have on the development of the countries' shipping industries are given. This analysis cannot be conclusive, as the process of liberalization and privatization is not yet terminated. In addition, policy reform programmes can only provide a framework within which competitive shipping companies can develop and within which transport systems can increase efficiency to the benefit of the trading community. This has to be a dynamic framework that remains responsive to general economic developments and to the specific needs of the actors in the maritime transport markets. It can thus be expected that further changes will occur in the overall management and support of the process of progressive liberalization embarked on, without, however, reversing the general policy direction.

106. Furthermore, it is rarely possible to construct a monocausal relationship between policy reform and specific market developments. Rather, it seems safe to assume that a number of external and internal factors are at the root of the sometimes bleak situation that the maritime industries of NIS countries face today.

A. Impact of policy measures on the participation of national fleets in shipping

(i) Loosening of cargo reservation

107. Before the introduction of shipping policy reforms, State-owned companies operated under the cover of protectionism and did not compete for cargo. Cargo was allocated to them according to centrally adopted plans and sailing schedules. With the dramatic change in policy and the resulting absence, or at least loosening, of reservation measures, they find it very difficult, if not sometimes impossible, to compete successfully for cargo. As a result, these companies experience difficult times and often feel that they are "victims" of the new shipping policy, and it sometimes appears that they support ideas of reintroducing some sort of a reservation scheme, even if only as a temporary measure to facilitate a stable transition to market conditions. However, bearing in mind the countries' obligations to the world community, there is a general consensus not to resort to any reservation arrangements as a strategic policy instrument based on legislation that allocates national foreign trade commodities to domestic carriers. In Russia, one alternative that has been suggested is to issue temporary licences for national carriers to transport specified foreign trade commodities, excluding cases when adequate national tonnage is not available or when licensing runs counter to government obligations. It is also implied that no measures shall be implemented without advising partners and competent international organizations, consultations and negotiations on, *inter alia*, the advisability of temporarily invalidating those provisions of the agreements and conventions to which possible measures may be contradictory.

(ii) Financial constraints

(a) Reduced government support

108. As previously stated, government financial support has been dramatically reduced or even discontinued. Budget financing may cover publicly available operations of ice-breakers and passenger vessels, hydrographic enterprises, communications systems, the salvage-coordination centres, educational establishments, etc., but, in conditions of increasing liberalization and competition, this sort of aid does not fill the financial vacuum in which former State-owned shipping companies find themselves.

109. Without government aid, shipping companies cannot purchase vessels, replace obsolete ones, or even cover current expenses. Other sources of external finance, like the capital market and various financial institutions, are either

not available to them or are greatly limited. And so, because of their inability to finance fleet expansion, modernization and operations, their existence is threatened by the withdrawal of government assistance.

(b) A decrease in hard currency net revenues

110. Net revenue in hard currencies have dropped significantly, mainly because of a reduction in the cargo volume carried, coupled with increased expenses for bunkering and ship-repair abroad. Furthermore, the increasing tendency to flag out vessels has influenced net revenues. Reductions based on this latter phenomenon, however, are primarily of a statistical nature.

111. Equally important is customers' non-payment of freight,[12] which accounts for the fact that the most capital-intensive shipping companies not only have become or are becoming non-profitable, but also are even on the edge of bankruptcy, despite the fact that at the same time the so-called hard currency efficiency of tonnage utilization (revenue in United States dollars per 1,000 dwt/day) has grown.[13]

112. As a consequence, the shipping companies' fleets shrink, are threatened by economic and technological obsolescence and, consequently, are not in a position to compete effectively (table 5).

113. In order to put an end to this process and start a real renovation and replenishment of tonnage, the scarce finances of shipping companies need to be supplemented at this stage, first by government resources. Otherwise, it is difficult to remedy the situation and put companies in a position to compete effectively even in national shipping markets, let alone in cross-trades.

---

[12] In Russia, the freight debt of customers to shipping companies was 73.7 billion roubles in 1994.

[13] The hard currency efficiency of tonnage utilization in Russia in the first half of 1994, as compared with the similar period of 1993, rose by 6 per cent and reached US$ 188.6 per 1,000 dwt/day.

Table 5

Qualitative indicators of the Russian fleet
(1991-1994)

Indicators	1991	1992	1993	1994 (estimated)
1. Transport fleet				
number of ships	799	776	696	680
tonnage (thousand dwt)	10 508	10 224	9 004	8 954
2. Deletions of obsolete tonnage from the national fleet				
number of ships	49	34	95	31
tonnage (thousand dwt)	455	324	1 370	400
3. Additions to the national fleet				
number of ships	12	11	15	15
tonnage (thousand dwt)	55	51	139	352
4. Average age (years)	16.9	17.4	18.3	19.0
5. Number of operating ships beyond the "normative" a/ life of service				
number of ships	298	308	315	351
tonnage (thousand dwt)	2 059	2 592	2 610	3 290
6. Expenditures for repair, spare parts and technical maintenance of ships (billion roubles)	0.65	26.3	159.0	500-600
including hard currency (billion roubles)	0.25	22.2	114.0	300-450

a/ "Normative", as determined by the Ministry of Transport of the Russian Federation. Thus, the tonnage concerned is considered obsolete and should have been removed from the national fleet.

(iii) Reduction in the carriage of national foreign trade

114. Along with the decrease of the relevant countries' tonnage, they have lost their position in the carriage of cargo. In Russia, the volume of cargo carried by the national transport fleet decreased from 98.8 million tons in 1991 to 81.5 million tons in 1993. In 1994, it is estimated to be 65.0 million tons and in 1995, 62.0 million tons. If overseas trade only is considered, the volume of cargo fell from 76.2 million tons in 1991 to 69.6 million tons in 1993. In 1994, it is estimated at 58.0 million tons and in 1995, at 56.0 million tons. During the period of centrally planned economies, their fleets were assured of cargo flows and, consequently, of a stable cargo base for their development. Now national fleets must compete for national foreign trade cargo and in cross-trade. In other words, they have no cargo guarantees for their promotion and in a few cases the results are disastrous.

115. In addition to the depressed condition of national tonnage, other negative factors have affected the situation, including: the general economic recession

and an alteration in terms of shipment in favour of foreign shipowners. The NIS countries experience considerable difficulties regarding the present general economic situation. The deep, prolonged and widespread crisis has caused a significant decrease in aggregate economic activity and in the volume of cargo flows, which is aggravated by changes in terms of shipment. In centrally planned economies, governments had administrative devices to ensure that c.i.f. terms were used for exports and f.o.b. terms for imports. These practice had an impact similar to a reservation scheme and meant that national tonnage of the countries concerned carried cargo guaranteed by the government without any competition. Now, the shipment terms are freely negotiated, resulting in drastic alterations, to the advantage of foreign shipping companies, which now carry an increasing portion of foreign trade cargoes of all NIS countries.

116. Finally, the volume of commodities being carried has fallen because of non-payments of freight by domestic customers, and therefore, cargo is now accepted for transportation on some trade routes only if prepaid.

B. Impact on freight rates

117. Freight rates for the carriage of export-import commodities have fallen dramatically. But it is very difficult to identify a causal relationship between liberalization, other shipping reforms and tariff rates. Reasons are multifarious, including the continuing general overcapacity and depression of freight markets. Thus, in 1992-1994, freight rates for petroleum recommended by the Russian Ministry of Transport for orientation of local shipping companies fell in the trade routes of Novorossiysk-Turkey by 24 per cent, of Novorossiysk-Italy by 19 per cent and of Novorossiysk-United States by 27 per cent. The reason for this, however, can be seen primarily in the state of the freight market.

C. Impact on quality of services

118. There are a number of indicators to assess quality of services. In this context, reference is made to the age of vessels, an indicator for their suitability for different trades, and to safety of navigation. Available tonnage is getting old and age has an adverse impact on the qualitative level of services.

119. A level of safety was achieved through the system within which activities of State-owned shipping companies were strictly controlled by central government agencies, thus ensuring a relatively high level of safety of navigation. Transition of the countries to market economies has involved, among other things, the entry into the market of many small and medium-sized private shipowners and operators. This has often occurred on a short-term speculative basis, without ensuring the provision of stable and reliable services. Maintenance of ships and matters of safety often appear to be of minor importance to them. This is confirmed during inspections of vessels in ports of States members of the Paris Memorandum.[4]

120. To remedy the situation, various measures are being taken, including stricter control over vessels, regardless of their ownership, in terms of their compliance with domestic and international safety norms. It is also instituted that any potential carrier must receive a licence to transport commodities, and the condition of his ships and arrangements for ensuring safety within the company are to satisfy requirements of domestic and international standards. In addition, measures are being introduced in respect of effective implementation of international standards in merchant shipping. It is expected that these and other measures will finally improve the situation in the field of navigation

---

[4] The rate of detention of ships flying flags of NIS increased dramatically over the years. The actual detention rates were as follows: 0.7 per cent in 1990 (USSR flag); 1.2 per cent in 1991 (USSR flag); 2.5 per cent in 1992 (NIS flags); and 7.3 per cent in 1993 (NIS flags). Source: The Memorandum of Understanding of Port State Control, Annual Reports, 1992 and 1993.

safety which is closely connected with the competitive position of the shipping industries of the NIS.

D. Impact on management and interaction with other modes of transport

121. Organizational structures of management typical of former State-owned shipping companies in many cases have not changed or have changed only marginally, despite their transformation into joint stock companies and in spite of new market conditions that impose an urgent need for restructuring to increase competitiveness. The major practical difference may be the absence of links with a government agency when employment contracts are concluded with the top management of a shipping company. There is also no need to observe regulations concerning State-owned enterprises.

122. Furthermore, it is obvious that a competitive position depends on the costs of services rendered by shipping companies, a fact that is often disregarded by the countries' shipowners. The principal incentive for shipping companies' employees, who are often also major shareholders, is still regular pay and regular pay increases. The consequence of this is twofold. Apart from the direct impact on the cost of services rendered, companies cannot satisfy requirements of capital in terms of remuneration nor even earn the income needed to broaden their capital base or create reserves for replacement, let alone for new investments in vessels. This attitude also contributes to maintaining the slow pace of converting joint stock shipping companies (former State-owned companies) into private, commercially oriented shipping companies not burdened by activities that a shipping company does not typically engage in.

123. One of the results of privatization and liberalization is that the former administrative system of maritime transport management and long-term smooth economic and technological ties with other transport modes and shippers have become disrupted. As a consequence, many problems arise, especially at the interface with railways. Therefore, as a way out, some attention is being paid to freight forwarding and the setting up of a freight-forwarding system, as freight forwarding is an essential component of a rational overall transport system that provides reduced overall transport costs, timely delivery of commodities, security of cargo and improved payment procedures.